

2010

ANNUAL REPORT

BUILDING THE  
FUTURE ON SOLID  
FOUNDATIONS



Centre de réajustement  
des Québécois

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## **Building the future on solid foundations**

In 2010, we successfully met commitments made earlier this year with our five strategic priorities.

We worked closely and in a concerted manner with our depositors to achieve the objectives derived from our priorities and build solid foundations for the future.

The next chapter opens with a major challenge: harness the Caisse's full potential to create an effective and agile organization that can fulfill its mission in a complex economic environment.

# 2010 at a Glance

## 13.6%

### THE CAISSE'S OVERALL RETURN

The three major asset classes contributed to this result:

- Fixed income: 9.7%
- Inflation-sensitive investments: 16.3%
- Equity: 14.6%

## 9 out of 11

### SPECIALIZED PORTFOLIOS

These actively managed portfolios outperformed their benchmark index or added value.

## \$151.7 B

### \$80.1 B INCREASE IN NET ASSETS

Attributed to net investment results of \$17.7 billion and \$6.4 billion in net deposits.

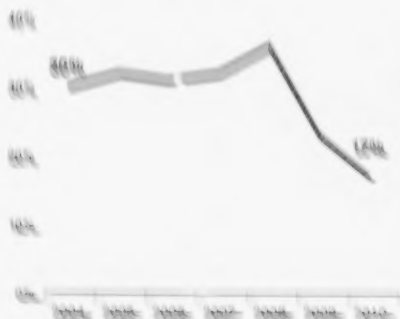
## 19.5%

### REDUCTION IN LIABILITIES FROM \$39.1 BILLION TO \$31.5 BILLION

This reduction helped strengthen the Caisse's financial position.

### HISTORY OF LIABILITIES

(as a percentage of total assets)



## \$3 B

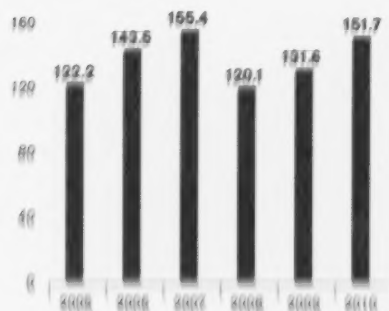
### SOLID FINANCIAL POSITION

A \$2 billion term note issue for the Canadian market in January 2010.

A €750 million term note issue for the European market in June 2010.

### CHANGES IN THE CAISSE'S NET ASSETS – 2005-2010

(in billions of dollars)



## \$45 M

### REDUCTION IN OPERATING EXPENSES

Down 18% over two years.

## AAA

### HIGHEST CREDIT RATINGS MAINTAINED

DBRS, Moody's and S&P once again awarded the highest credit ratings – with a "stable" outlook – to the Caisse and CDP Financial.

Significant reduction in risk

**56%****ACTIVE RISK**

Drop in the overall portfolio's active risk – from 10.3% to 4.5%.

**54%****ABTN**

Decrease in the ABTN portfolio's market risk.

**10%****ABSOLUTE RISK**

Drop in the overall portfolio's absolute risk – from 38.1% to 34.3%.

**13.2%**  
to  
**14.3%**

**RETURNS OF  
MAJOR DEPOSITORS**

In 2010, the returns of the Caisse's seven main depositors ranged between 13.2% and 14.3%.

**25****DEPOSITORS**

The Caisse serves 25 depositors, primarily Québec public and private sector pension and insurance plans. As at December 31, its seven main depositors held 95.5% of net assets.

**NET ASSETS OF THE SEVEN MAIN DEPOSITORS**

(as at December 31, 2010)

	2010	
	\$M	%
Government and Public Employees Retirement Plan (RREGOP)	41,301	27.2
Fonds d'amortissement des régimes de retraite (FARR)	34,202	22.6
Fonds du Régime de rentes du Québec	33,845	22.3
Supplemental Pension Plan for Employees of the Québec Construction Industry	12,047	8.0
Fonds de la santé et de la sécurité du travail	9,563	6.3
Fonds d'assurance automobile du Québec	7,006	4.6
Pension Plan for Management (RRPE)	6,843	4.5
<b>Total of the seven main depositors</b>	<b>144,807</b>	<b>95.5</b>
Other	6,935	4.5
<b>Total</b>	<b>151,742</b>	<b>100.0</b>

## 2010 at a Glance

# Collaborating Performing

IN A SUSTAINED WAY  
WITH OUR CLIENTS

- 150 meetings with our depositors, portfolio managers and members of senior management
- Four information seminars on risk, economic outlooks and the new portfolio offering
- Four consultation and discussion forums between depositors and members of senior management
- Significant improvement in monthly reports to depositors
- New semi-annual newsletter dedicated to risk
- Team work in order to review and adapt each depositor's investment policy while taking into account its issues and the new portfolio offering

BY DELIVERING A  
SOLID 13.6% RETURN  
TO OUR CLIENTS

- A \$20.1 billion increase in net assets – for a total of \$151.7 billion
- \$17.7 billion in net investment results
- 9 of the 11 actively managed portfolios outperformed their benchmark index or added value
- Returns ranging between 13.2% and 14.3% for the seven main depositors

# Mastering

RISKS AND FOCUSING  
ON OUR CORE BUSINESS

- Selection of high-quality assets
- Agile portfolio management in a volatile market
- Orderly sale of non-core assets in our investment strategy
- 10% reduction in the Caisse portfolio's absolute risk and a decrease of over 50% in its active risk
- 54% reduction in the market risk of the ABTN portfolio
- Realization of large scale projects to improve the risk management tools and implement new frameworks and processes

# Investing Ourselves

TO SERVE OUR CLIENTS  
AND QUÉBEC

- A greater presence in Québec through our knowledge of the Québec market and the concerted efforts of our teams
- A \$3 billion increase in the Caisse's total assets in Québec
- A portfolio offering significantly revamped and launched over six months to benefit our depositors
- Five strategic priorities carried out with rigour and discipline to strengthen the Caisse's foundations



# Messages from the Chairman and from the President and Chief Executive Officer

# Message from the Chairman

For the Caisse de dépôt et placement du Québec, 2010 was a year of continuity, with the implementation of strategic priorities and initiatives identified during the second half of 2009. From a governance standpoint, the Board is pleased to note significant progress in achieving these new priorities aimed at rebuilding the Caisse's foundations. Moreover, the institution's solid financial results and remarkable progress spring from the concerted effort of the Caisse's teams to make this organization efficient and firmly turned to the future.

During the past year, the quality of the relationship between the Caisse and its depositors remained one of the Board's top priorities. From this perspective, it should be noted that we implemented a new collaborative model to ensure this relationship takes place in a climate of transparency and trust. In the process, the Board approved the fundamental reorganization of the Caisse's portfolios to better suit the performance objectives, risk tolerance and asset allocation of the depositors.

## ENHANCED RISK MANAGEMENT

The Board strongly supported the continued improvement of the Caisse's risk management and is also very satisfied with the progress in this area. With the support of the Board's Risk Management Committee and the close collaboration of the senior management team, the Caisse strengthened its risk management tools and processes with the adoption of best practices.

In addition, the Board is pleased that rating agencies Standard & Poor's, Moody's and DBRS confirmed the Caisse's credit ratings, citing among others its enhanced risk management and financial strength.

## GREATER CONTRIBUTION TO ECONOMIC DEVELOPMENT

In terms of economic development, it is clear for the Board that the deployment of a robust action plan led to compelling results, strengthening the Caisse's presence in Québec. This leaves no doubt that this institution can play a leadership role in the province's economic development, benefiting its depositors and Québec.

## A FULLY COMMITTED BOARD

As Chairman of the Board, I would like to mention the significant contribution of Board members. They have shown constant commitment. They brought their diverse expertise to serve the Caisse and were always available for both regular and special meetings. I wish to particularly acknowledge the work done by members of various committees who, through their rigorous analysis and valuable input, enriched and guided the Board's discussions.

Accordingly, the Audit Committee oversaw the compliance of financial statements, strictly monitored the internal audit and reviewed the many reports received during its mandate. The Human Resources Committee established a new compensation policy based on best industry practices and established a framework to recruit, retain and motivate highly qualified personnel.

Finally, the Governance and Ethics Committee reviewed the institution's responsible investment policy and continued to examine the governance and ethics policies and practices that make the Caisse a recognized leader in these areas.

The Board can also rely on its effective and transparent relationship with the Caisse's senior management. This communication is crucial – it allows the Board to be apprised of important issues promptly and have vital information and documentation for informed decision making. This relationship was crucial to the success and progress of our various initiatives in 2010.

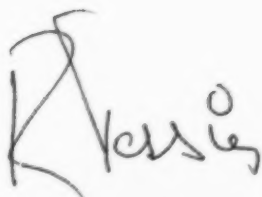
## OUR PROGRESS. OUR FUTURE.

The Caisse's achievements in 2010 were also due to employees who brilliantly met their goals in an atmosphere of renewed confidence. We would like to thank them for their loyalty and commitment.

Overall, the Board believes that the Caisse made progress on all fronts. The financial results testify to this fact. The Board encourages the entire team to pursue the work under way with energy and to build a strong organization striving to improve its management in order to deliver, over time, the results expected by its depositors.

In closing, I would like to thank the President and Chief Executive Officer, Michael Sabia, and his management team, whose accomplishments far exceeded targets. Making insightful decisions, implementing innovative initiatives and, above all, deploying an action plan focused on our strategic priorities truly characterizes 2010. The President and Chief Executive Officer had agreed earlier this year to be judged on a set of detailed and very demanding objectives, which were met and exceeded many times. For this, the Board has recognized him for his outstanding performance.

The Board is very pleased with the Caisse's financial performance. It will continue to support senior management in implementing the strategic plan to make the Caisse an organization that remains focused on long-term performance and guided by its priorities, to the benefit of depositors, Québec companies and Québec itself.



**ROBERT TESSIER**  
Chairman of the Board

# Message from the President and Chief Executive Officer

2010 was a year marked by economic and financial uncertainty. At the Caisse, we stuck to our basic principle of "common sense" that we have followed for the last couple of years: performance, client focus, rigour and simplicity.

This disciplined approach, I believe, enabled us to make a great deal of progress on our five strategic priorities aimed at strengthening the Caisse's foundations for the long term. Our efforts were aimed at a number of key issues:

- Collaborating with our clients
- Restructuring our portfolios
- Enhancing risk management
- Strengthening our presence in Québec
- Redesigning our internal operations
- Improving our balance sheet

With rigour and discipline, our teams have refocused the Caisse on its core areas of expertise and, by emphasizing the importance of high-quality assets, they managed to navigate a difficult-to-predict landscape.

Thanks to their efforts, the Caisse is healthy again.

What strikes me most about our performance in 2010 is that the Caisse team clearly demonstrated its ability to execute an ambitious strategic plan while generating solid returns. In the coming years, facing an uncertain, volatile environment much like today's, this execution capability will be fundamental to our success.

Many significant economic changes are under way worldwide – changes that offer as many opportunities to earn returns as to make costly mistakes. This will be an environment that demands vigilance and a capacity to understand underlying trends both in the near term and over the long run. The Caisse, like all investors, will have to remain very attentive to these shifts over the next 12 to 18 months – and especially over the longer term – to grasp their scope and better understand their significance.

## IN THE SHORT TERM: TWO OPPOSING FORCES

2010 was the second year of recovery after the 2008 crisis. Up until now, renewed growth required support from public authorities, at least in developed countries. Such support has exceeded US\$2 trillion and largely contributed to the stock market rebound in the latter part of the year.

In 2011, however, we expect a deceleration in growth due to the removal of economic stimulus, debt reduction by consumers and governments in developed countries, tighter monetary policies in developing countries as a response to higher commodity prices, and austerity measures in overly indebted eurozone countries.

Two major trends will then struggle for dominance.

On the one hand, the marked improvement in several key economic indicators suggests that the renewed growth will continue for some time. In Québec, the infrastructure program launched before the economic crisis has supported growth, which helped eliminate the gap between unemployment rates in Québec and the rest of Canada for the first time in recent history. In North America, a significant improvement in corporate profits largely explains the increase in business confidence. In this environment, non-residential private investment is increasing rapidly and the employment situation continues to improve. All in all, this trend suggests that the recovery – albeit uneven – will persist despite volatility and lingering uncertainty.

On the other hand, this benign scenario is challenged by the persistence of worrisome downside risks. For example, will geopolitical changes in North Africa and the Middle East significantly disrupt oil production? Is political cohesion in Europe robust enough to ensure that austerity efforts are equitably shared? Will measures by the People's Bank of China to ease inflationary pressures be successful? Will U.S. residential real estate finally show signs of stabilization?

The struggle between these two opposing forces will continue over the next 12 to 18 months. In our view today, it is very difficult to predict which of these tendencies will prevail. For that reason, remaining vigilant and agile will continue to be our top short-term priority.

If the moderate growth trend weathers the storm over the next 18 months, markets will nevertheless be buffeted by the consequences of the predictable exit strategies of public authorities, including both tightening monetary supply and government budget cuts. Of course, these impacts and their timing are likely to vary by region. Europe is already moving in that direction. In the United States, a fiscal adjustment will likely be initiated only after the next election. The Bank of Canada may resume its tightening cycle, while avoiding major policy differences with the U.S. Federal Reserve.

### **AGAINST THIS BACKDROP, LONG-TERM STRUCTURAL CHANGES**

Market developments over the next 18 months will occur against a backdrop of profound structural changes in the global economic and financial environment. Every investor and every major economic bloc will be confronted with this reality.

#### **Developed countries**

G7 countries are facing major declines in labour growth rates that will create downward pressure on economic growth. Relative to the last five years, this will represent a slowdown of about 0.3% to 1%. It would be very surprising if other measures, such as productivity improvements, manage to compensate for the totality of this decline. Nevertheless, such measures remain necessary.

Moreover, current sovereign debt levels in these countries are unprecedented. In Japan and the United Kingdom, gross total debt is now 450% of GDP. For the United States and Europe's peripheral nations, it is approximately 300% of GDP. Whatever its magnitude, the debt reduction process will be long and painful.

Developed countries also face major trade imbalances, including large current account deficits between the U.S. and China, and in Europe. Imbalances on this scale have never been seen before.

#### **Emerging countries**

In contrast, more than 50% of global growth over the next five years will come from emerging countries, driven by rapid population growth and rising per capita GDP. This growth will be coupled with massive urbanization in Asia. From 2010 to 2030, some 800 million people will migrate to urban centres and the size of the middle class in China and India will explode. The impact on global energy and resource demand will be considerable. This massive increase in demand for commodities will benefit Québec and Canada, since we have an abundance of such resources. It will also pose a serious challenge: striking a balance between resources and other sectors.

Consumption patterns will also change in emerging economies, generating long-term demand in the agricultural, industrial and manufacturing sectors. However, supply constraints with respect to many resources and raw materials may continue to drive up operating costs. Finally, inflation will remain a major challenge of the new global economy.

So, can the world afford the growth it needs? Growth in emerging countries is still a major trend, but the rebalancing of the global economy is not yet a done deal and raises important questions from a social and political standpoint. For instance, China's 12th five-year plan, which aims to ensure that national growth is less dependent on foreign trade and investment and more focused on domestic demand, is facing many challenges and raises a host of social and environmental issues.

### **THE KEY TO THE CAISSE'S SUCCESS**

How can the Caisse successfully fulfill its mission in a changing and complex world both in the short term and in the years to come? At a minimum, I think we will need three things.

## Message from the President and Chief Executive Officer

### A BETTER UNDERSTANDING OF THE FUNDAMENTALS

It will be essential to stay disciplined and continue to invest where we have comparative advantages, for instance, in Québec. We must also develop a deeper understanding of the broader world that can be factored into day-to-day portfolio investment decisions. In that sense, greatly advancing our fundamental research capabilities has become an essential priority. Mathematical techniques alone are not sufficient to evaluate issues that are often qualitative in nature and demand judgment. An enhanced research capacity will be a vital tool for identifying sectors and markets with high growth potential, implementing appropriate strategies and making the right choices to generate long-term returns.

At the same time, an enhanced research capability will enable us to strengthen our risk management. Not only will we continue to closely monitor "conventional" risks, but we will also conduct more in-depth assessments of risks related to the economic, financial and political environment. To that end, in addition to the rigour and accuracy of our existing calculation methods and analytic tools, we will need to rely on informed, good judgment, based on a broader, more global view.

### A PARTNERSHIP STRATEGY

As well, we will consolidate and further develop our alliances with partners worldwide in order to make profitable investments for our depositors. Our strategy will place an emphasis on partnering with local stakeholders in promising markets where we plan to invest, so that the Caisse can benefit from their finer understanding of the market in question. We believe that the development of our global networks and multiple partnerships will also enable us to better support the international expansion plans of promising Québec companies.

### THE EXPERTISE OF OUR TEAMS. A CORNERSTONE FOR THE FUTURE.

The Caisse's success ultimately depends on the expertise, talent and commitment of our people. Those qualities are very much evident at the Caisse, as reflected by our solid 2010 results. Our people will continue to make the difference in the future. Given the intense competition for professional expertise in today's global financial markets, talent retention and recruitment will remain one of our top priorities.

With their rigorous and disciplined approach, our people possess the capabilities required to identify and seize real investment opportunities – not investment fads – that will create value for the next 10 or 15 years and provide the source of depositor returns.

In this way, we will realize the Caisse's full potential to continue meeting the long-term needs of depositors and supporting the growth of Québec companies.

Ultimately, what matters to us is the long run. Because we are in a marathon, not a sprint. The Caisse is here for the long haul.



**MICHAEL SABIA**  
President and Chief Executive Officer

# Our Clients, the Depositors

# Our Clients, the Depositors

## CLOSE COLLABORATION WITH OUR CLIENTS

In 2010, the Caisse took several steps that profoundly changed how it works with its clients, the depositors. These actions reflect the commitments made by the Caisse in 2009 to be closer to its clients and better meet their needs. The aim is to encourage more sustained and diverse interactions, more transparent and constructive exchanges, and a deeper understanding of each other's perspective.

### HIGHLIGHTS

**01** Depositors' net assets increased by \$20.1 billion in 2010 due to net investment results of \$17.7 billion and \$2.4 billion in net deposits.

**02** Caisse and depositor teams worked closely to make major changes to the portfolio offering.

**03** In 2010, depositor reporting improved significantly, primarily through the addition of new information newsletters and the enhancement of existing regular reports.

**04** In 2010, the Caisse diversified and greatly increased the number of opportunities for exchanges between its teams and those of its depositors.

Deployment of the 2010 initiatives was based on close collaboration between the teams of the Caisse and its depositors. They focused on three areas of improvement:

1. Establishing a new collaboration model.
2. Launching a new portfolio offering.
3. Improving the quality and clarity of the reporting.

### NEW COLLABORATION MODEL

For the Caisse, close collaboration between its advisory teams, portfolio managers and depositors is essential to fulfill its mandate. As a result, in 2010, it significantly increased the number of opportunities for exchanges and information sharing with its clients. For example:

- Some 150 meetings allowed depositor representatives to interact directly with the Caisse's managers and executives.
- Four seminars were held during the year. In addition to information sessions on risk management and the economic outlook, two one-day meetings focused on various aspects of the Caisse's new portfolio offering.
- Created in 2010, four quarterly consultation forums were attended by representatives of seven major depositors, the President and Chief Executive Officer and members of the Caisse's senior management team. The topics at these meetings touched upon the challenges of the depositors and the Caisse.

The Caisse also enhanced its advisory services by offering its asset-liability matching expertise to depositors who requested it. It adjusted its service offering to consider the risks associated with the liability of these depositors.

Finally, in 2010, the Caisse took the initial step in reviewing depositors' service level agreements. Thus in collaboration with main clients, the Caisse defined the outline of a model agreement that establishes, in particular, the following elements:

- Roles and responsibilities between the Caisse and its depositors.
- The Caisse's service offering to depositors.
- The management framework, including investment policies for each specialized portfolio and the integrated risk management policy.
- Reporting and communication procedures.

During 2011, the next step for the Caisse will be to use this model to conclude a customized service level agreement with each depositor.

## NEW PORTFOLIO OFFERING

The Caisse aims to provide investment products and advisory services best suited to the needs and long-term objectives of its clients. In 2010, this is what prompted a fundamental change and, in turn, a simplification and clarification of its portfolio offering, including new investment options and risk hedging.

Caisse and depositors teams worked closely together to make these changes. Every element of the portfolios was reviewed: asset composition, management style, performance and value-added targets, and portfolio management supervision.

This revised portfolio offering now gives more flexibility and transparency. It is easier for depositors to establish their asset mix and, if they want to, better match it to their liabilities.

To learn more about the changes to the Caisse's specialized portfolio offering, please refer to pages 23 and 24.

To learn more about the Caisse's overall portfolio, please refer to pages 25 to 29.

## ENHANCED REPORTING

Improving its reporting activities is one of the many measures taken by the Caisse in 2010 to strengthen the collaboration model with depositors. The information sent to depositors became clearer, more relevant and more transparent. It also led to significant improvements to existing reports and the launch of new tools during 2010:

- Reports' analysis and interpretation section were revised to promote better understanding of the different charts and graphs.
- A new monthly newsletter provides each depositor with a summary of information available on its returns and asset allocation.
- A new semi-annual newsletter is entirely devoted to risk and aims to explain the risks associated with various portfolios and asset classes and make the link with the risk component of the depositors' investment policies.

These documents complement the information provided by account managers at meetings with their clients.

## Our Clients, the Depositors

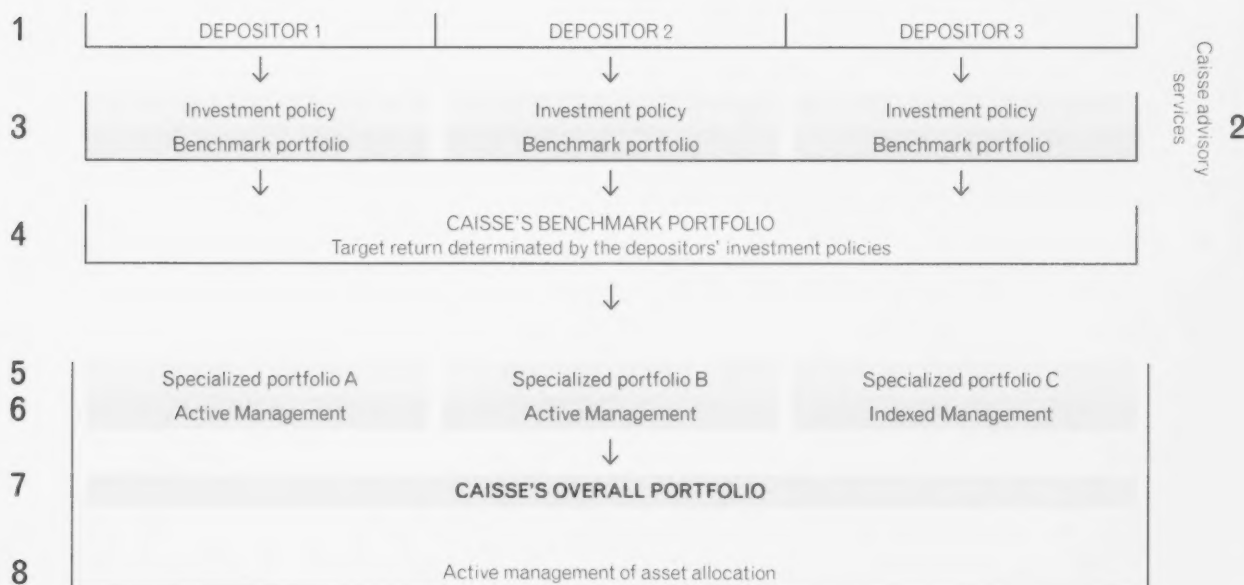
### COMPLEMENTARY ROLES

Below is an outline of the respective roles (depositors and Caisse) in regards to the management of the depositors' holdings (see Figure 1).

1. Depositors entrust their funds to the Caisse to make them grow, specifying their performance objectives, risk tolerance and asset allocation in their investment policy.
2. The Caisse provides depositors with investment advice, working closely with them to develop and revise their investment policy.
3. Each depositor has the opportunity to invest its funds in the Caisse's 17 specialized portfolios and select a target currency exposure. It can choose to invest in actively managed or indexed foreign equity portfolios. The asset allocation of a depositor (its choice of various specialized portfolios) becomes its benchmark portfolio.
4. The Caisse's benchmark portfolio is based on the weighted average of all depositors' benchmark portfolios.
5. The Caisse's portfolio managers invest the funds of the depositors in accordance with their investment policies and the investment policies of their specialized portfolios.
6. Eleven of the 17 specialized portfolios available to depositors are actively managed. The managers of these portfolios aim to outperform their benchmark through security, sector or country selection. Active management is concentrated where the Caisse has comparative advantages. The six other portfolios are indexed, and aim to replicate the benchmarks.
7. The aggregation of the depositors' funds represents the Caisse's overall portfolio. The return on this portfolio corresponds to the weighted average return on depositors' funds.
8. Given market conditions and the short and medium-term economic outlook, the Caisse carries out rebalancing activities, namely it adjusts the weighting of its specialized portfolios. The purpose of this exercise is to improve the performance of the depositors' funds and, consequently, the Caisse's overall portfolio.

FIGURE 1

### PROCESS USED TO MANAGE DEPOSITORS' HOLDINGS



DEPOS

In 2010, t  
private s

STOR

The Commission has 20 depositors, primarily Québec public sector pension and insurance plans.

Table 2 lists the seven main depositors holding 95% of depositor net assets as of December 31, 2010. Table 3 presents the 25 depositors and bodies that administer them, including a comparison of net assets as at December 31, 2009 and December 31, 2010.

TABLE 2

THE SEVEN MAIN DEPOSITORS

	Depositor	Type of plan	Description
1	GOVERNMENT AND PUBLIC EMPLOYEES RETIREMENT PLAN (RREGOP)	Pension plan	RREGOP consists primarily of contributions by employees who work in Québec's health and social services sector, education system and public sector. The plan is administered by the Commission administrative des régimes de retraite et d'assurances (CARRA).
2	FONDS D'AMORTISSEMENT DES RÉGIMES DE RETRAITE (FARR)	Pension plan	FARR provides for payment of retirement benefits that are the responsibility of the government, according to the provisions of the retirement plans for the public and parapublic sectors. The fund is managed by the Québec government and administered by the Commission administrative des régimes de retraite et d'assurances (CARRA).
3	FONDS D'AMORTISSEMENT DES RÉGIMES DE RETRAITE (FARR)	Pension plan	The fund is administered by the Commission administrative des régimes de retraite et d'assurances (CARRA). The fund is managed by the Québec government and administered by the Commission administrative des régimes de retraite et d'assurances (CARRA).
4	SUPPLEMENTAL PENSION PLAN FOR EMPLOYEES OF THE QUEBEC CONSTRUCTION INDUSTRY	Pension plan	The plan is administered by the Commission administrative des régimes de retraite et d'assurances (CARRA). The contributions to the plan are paid by construction industry employees and workers.
5	FONDS DE LA SANTÉ ET DE LA SÉCURITÉ DU TRAVAIL	Insurance plan	The fund mainly compensates workers who have had work-related accidents and contributes to their rehabilitation. The fund is administered by the Commission de la santé et de la sécurité du travail (CSST) and financed by contributions from Québec employers.
6	FONDS D'ASSURANCE AUTOMOBILE DU QUÉBEC	Insurance plan	The fund compensates victims of vehicular accidents and promotes traffic safety. It is financed mainly by fees collected by the Société de l'assurance automobile du Québec (SAAQ) for driver's licenses and vehicle registration.
7	PENSION PLAN FOR MANAGEMENT EMPLOYEES (PMP)	Pension plan	The PMP consists of contributions by management employees in the public and parapublic sectors. The plan is administered by CARRA.

ANNEXE 1

## THE CAISSES-DEPÓSITORS AND THE BODIES THAT ADMINISTER THEM

(en millions de dollars) (in millions of dollars)

	Fin 1999	Financement et investissements			
		2000	2001	2002	2003
<b>FINANCIAL</b>					
<b>Régie des rentes du Québec</b>					
Fonds de retraite du Québec	195	2385	223	2575	255
<b>Commission de la construction du Québec</b>					
Supplemental Pension Plan for Employees of the Québec Construction Industry	1971	12047	80	10571	80
<b>Commission administrative des régimes de retraite et d'assurances</b>					
Government and Public Employees Retirement Plan	1973	41301	27.2	37555	38.2
Pension Plan for Management	1973	5843	45	6432	49
Individual Plans	1977	173	0.1	316	0.2
Pension Plan for Elected Municipal Officials	1989	156	0.1	139	0.1
Régime de retraite pour certains employés de la Commission scolaire de la Capitale	2006	38	-	36	-
Régime de rentes pour le personnel non enseignant de la Commission des écoles catholiques de Montréal	2007	232	0.2	231	0.2
Régime de retraite des membres de la Sûreté du Québec - caisse participants	2007	191	0.1	68	-
Régime de retraite des membres de la Sûreté du Québec - caisse employeurs	2009	142	0.1	128	0.1
Régime de retraite des employés en fonction au Centre hospitalier Côte des neiges	2010	67	2	-	-
Régime complémentaire de rentes des techniciens ambulanciers/paramédics et des services préhospitaliers d'urgence	2011	227	0.2	187	0.2
<b>Ministère des Finances, Gouvernement du Québec</b>					
Fonds d'investissement des régimes de retraite	2011	21229	22.6	20110	21.9
Régime de retraite de l'Université du Québec	2011	210	0.1	22	0.1
Régime de retraite du personnel de l'UQAM	2011	20	1	4	-
Régime de retraite de l'Université de Moncton	2011	10	1	2	-
Régime de retraite de l'Université de Sherbrooke	2011	10	1	2	-
Régime de retraite de l'Université de Saint-Jérôme	2011	10	1	2	-
<b>REGIMES DE RETRAITE</b>					
<b>Régie des marchés agricoles et alimentaires du Québec</b>					
Fonds d'assurance agricole	195	2	-	5	-
<b>La Financière agricole du Québec</b>	196	247	0.2	232	0.2
<b>Assurance des marchés financiers</b>	199	538	0.4	493	0.4
<b>Commission de la santé et de la sécurité du travail</b>					
Fonds de la santé et de la sécurité du travail	1973	5593	0.3	6344	0.3
<b>Société de l'assurance automobile du Québec</b>					
Fonds d'assurance automobile du Québec	1978	1008	4.8	6103	4.7
<b>Fédération des producteurs de bovins du Québec</b>	1981	6	-	5	-
<b>Régime de rentes de survivants</b>	1987	384	0.2	347	0.1
<b>Conseil de gestion de l'assurance parentale</b>					
Parental Insurance Fund	2000	6	-	5	-
<b>OTHER DEPOSITORS</b>					
<b>Office de la protection du consommateur</b>	199	61	-	45	-
<b>Société des alcools du Québec</b>	199	144	0.1	-	-
<b>Ministère des Finances, Gouvernement du Québec</b>					
Fonds des générations	2011	8987	0.9	7946	1.8
Fonds de la réserve d'investissement de l'administration du Québec	2011	5	-	11	0.1
Fonds des cotisations de retraite accumulées	2011	249	0.9	181	0.6
<b>Total</b>		161148	100.0	151586	100.0

1 - Voir l'annexe 2 pour plus de détails.

2 - Les données sont présentées en millions de dollars. Les données sont arrondies à l'unité la plus proche. Les données sont présentées en millions de dollars.

# Management Report

# Macroeconomic Environment

## HIGHLIGHTS

**01** 2010: a year of recovery marked by significant instability.

**02** Europe's public finance crisis and conflicts in North Africa and in the Middle East impose risks on the global economy.

**03** Divergent interests between developed and emerging countries raise fears of a "currency war" and rising protectionism.

**04** To avoid a relapse of the U.S. economy, new monetary and fiscal stimulus measures were announced.

**05** Sustained economic recovery in Québec due to a favourable labour market and accommodative economic policies.

**06** The Canadian economy stands out for the strength of its domestic demand and rebounding commodities.

The global economic recovery solidified in 2010, although a climate of uncertainty remains in many respects. One thing is certain – a two-speed recovery has set in, with a clear distinction between the emerging and developed economies (see Figure 4).

The emerging economies, despite a sharp drop in growth in 2009, are now recovering rapidly. This is due to a combination of factors: a strong rebound in domestic demand, a recovery in exports, and a significant increase in investment. The developed economies, on the other hand, are still struggling with the effects of the financial crisis. The recovery is slower and more uncertain. The global economic recovery is therefore characterized by a clear distinction between the emerging and developed economies.

In the past year, most developed economies, led by the U.S., had to deal with the effects of household and financial sector debt reduction, resulting in a weaker recovery than in past recessions. Although the leading economic indicators of these countries improved, most are still below the peaks reached before the last recession. In addition, both in the U.S. and Europe, the climate did not improve enough to reduce the unemployment rate. The situation appears to be more positive in Canada, where the economic recovery made it possible to recover the jobs lost during the recession, and even to exceed the last cyclical peak achieved in 2006. Québec also held its own, creating nearly one third of the jobs in Canada, despite the competition issues raised by the strong Canadian dollar.

What does 2011 have in store? In the United States, the economy will benefit from the support of the monetary and fiscal stimulus measures announced at the end of 2010. In the eurozone, challenges posed by the precarious finances of certain countries and the banking system will slow down the recovery and increase substantial excess capacity, the key interest rates of which will remain at or close to historic lows. In addition, developed economies' core inflation will remain low despite a rise in oil prices. In any case, despite some pitfalls, the recovery should continue at a steady pace in 2011.

However, recent events could darken the economic outlook. First, if the conflicts shaking North Africa and the Middle East persist, intensify and spread to other petroleum-producing countries, the resulting surge in oil prices would undermine global growth. In addition, the March 2011 earthquake in Japan and its aftermath are creating uncertainty about the scale of the destruction to the country's productive capacity – and when its reconstruction can begin.

## DEVELOPED ECONOMIES

### Québec

The Québec economic recovery that began in spring 2009 continued in 2010 due to robust domestic demand and accommodating monetary and fiscal policies. The infrastructure program, which had allowed Québec to stand out from Canada as a whole during the crisis, continues to support growth. Higher profits and low interest rates fuelled the private investment rebound. In addition, the strong appreciation of the Canadian dollar favoured equipment imports, reducing acquisition costs.

The vigorous labour market, characterized by the creation of approximately 90,000 jobs since the end of last year, favourable credit conditions and an expanding real estate market drove household consumption. The Québec unemployment rate, higher than the Canadian level for many decades, ended the year at 7.5%, namely 0.1% lower than in Canada. Job creation in the health care and professional, scientific and technical service sectors contributed to this upturn.

Québec, which in 2009 had achieved real growth superior to that of Canada and the United States, performed well again in 2010 with growth of 2.8% compared with their performance of 3.1% and 2.9%, respectively.

### Canada

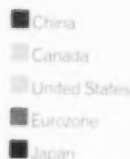
With 3.1% growth in 2010, the Canadian economy stood out from other developed economies for the vitality of its domestic demand and strong demand for commodities. It benefited from the global recovery throughout the year, particularly the recovery of the emerging economies, which largely explains the Canadian dollar's return to parity with the U.S. dollar. On the other hand, the rising

loonie and the strength of domestic demand contributed to surging imports and a deterioration of the balance of trade until the fall. An export rebound in the last months of the year, particularly in the energy sector, partly offset this phenomenon. This environment, positive overall, forced the Bank of Canada to initiate a monetary policy normalization process midyear and increase its key interest rate from 0.25% to 1%. However, the absence of inflation and the uncertainties surrounding the vigour and sustainability of the recovery prompted the central bank to halt its key interest rate hikes. Low interest rates and the employment recovery contributed to the ongoing increase in household debt and the rising real estate market. Against this backdrop, the Canadian economy's vulnerability to a sudden interest rate resurgence is increased. Given domestic demand, which should remain strong, the support of the monetary policy and improved U.S. economic outlook, the rebound nonetheless should continue, but at a slightly more moderate pace. Indeed, the strength of the Canadian dollar, the gradual withdrawal of fiscal stimulus measures and the risks related to heavy household debt loads will limit economic expansion.

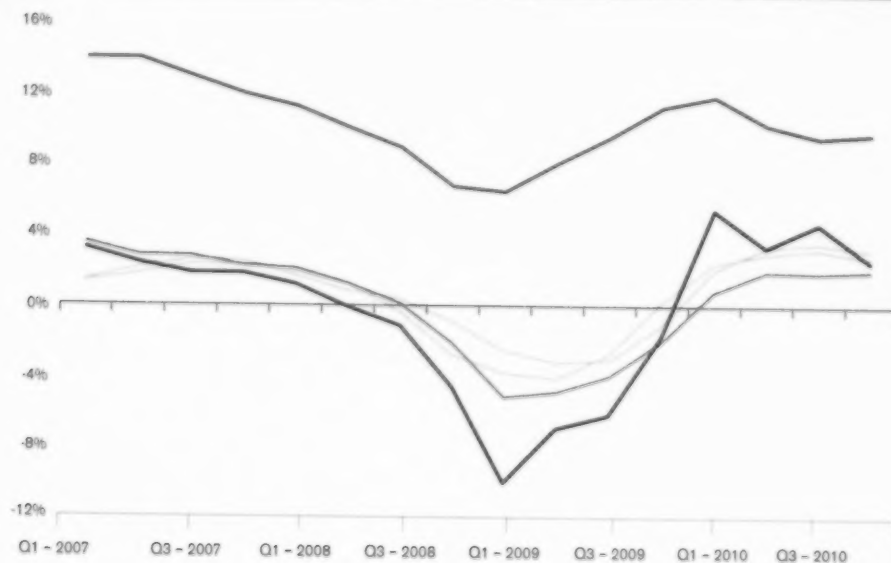
FIGURE 4

### GROSS DOMESTIC PRODUCT

(annual variation)



Sources: Economic Analysis and Asset Allocation Strategies, Datastream



## Macroeconomic Environment

### United States

The economic rebound was short term and relatively timid compared to the typical pattern of postwar economic recoveries. The 2.9% GDP growth in 2010 was not enough to lead to a substantial reduction in the unemployment rate, which was 9.4% at year-end. After a first half characterized by solid growth, the economy quickly showed signs of running out of steam, causing fears of a relapse to resurface. U.S. monetary authorities reacted promptly by launching a second quantitative easing plan, promising to acquire \$600 billion of federal government bonds by June 2011. The objective of this plan is to exert downward pressure on interest rates and, in turn, restart growth. The White House and Congress went further at the very end of the year, proposing new tax cuts and extending those already in place. These new stimuli will ensure significant support for the economy and favour the continuation of the recovery in 2011. However, some obstacles are looming on the horizon. Residential real estate is still in the grips of an oversupply of housing, fuelled by an ever-growing number of seizures and defaults. In addition, households reacted to the collapse of their financial nest egg by raising their savings rate and remain reluctant to use credit. Finally, the scope of budget issues and the political climate could convince various levels of government to reduce their spending.

### Eurozone

The eurozone showed surprising 1.8% growth in 2010, despite the public finance problems of certain countries on its periphery. While Germany was able to profit from the recovery of global trade, Greece, Ireland, Portugal and Spain saw their growth hindered by budget tightening, their lack of competitiveness and investor concerns about their government's solvency. The precarious public finance situation in these countries also plunged the financial markets into a period of instability in spring 2010. While the price of their bonds collapsed, the euro depreciated, and investors took refuge in the German and U.S. bond markets. The tension peaked in April 2010 when Greece, unable to borrow on the markets, had to request assistance from the European Union and the International Monetary Fund. This took the form of a €110 billion loan over three years, granted in exchange for the promise to undertake significant austerity measures. The Greek bailout induced these two entities, in May, to set up the European Financial Stability Facility, a €750 billion emergency fund to assist States in need. To reduce the tensions on the markets further, the European Central Bank also proceeded to purchase bonds of the indebted countries.

These decisions, historic in scope, were intended to defend the essence of the European Union as much as possible and create protection against any speculative attack. However, the eurozone crisis was far from resolved. In November 2010, Ireland had to ask for €67.5 billion of external assistance and, in exchange, the government had to commit to severe austerity measures designed to stabilize its debt and reduce its deficit. On April 8, Portugal has formally requested financial assistance from the European Union. In addition, the markets now fear that Spain will soon follow in the footsteps of Greece and Ireland. This climate of uncertainty explains why the European bailout plan could not alleviate the tensions in the bond markets and why the markets are still charging a very high risk premium to lend to the countries in difficulty. In this environment, the eurozone's economic outlook will be dimmed, due to the budget tightening that will affect the countries to varying degrees.

### EMERGING ECONOMIES

The growth surge in emerging markets, particularly in China and India, encouraged commodities prices to soar. Chinese economic growth continued at a lively pace, fed by the stimuli put in place during the crisis and the rebound in world trade. Nonetheless, accelerating inflation prompted the authorities to institute ever more restrictive measures to soothe inflationary pressures. These measures did not prevent China from obtaining an impressive 10.3% growth rate in 2010. India and Brazil posted growth rates of 8.6% and 7.5%, respectively.

In many emerging economies, vigorous growth, high interest rates and numerous investment opportunities are attracting foreign capital, which could lead to inflation and the appreciation of their currencies. In this environment, the extraordinary monetary easing conducted by the U.S. Federal Reserve in fall 2010 was denounced by the governments of these countries, which had to deal with the necessity of tightening their economic policies to contain overheating. They subsequently sought to stem the influx of capital by adopting various capital control policies. These measures have raised fears of a "currency war," which could lead to a global rise in protectionism.

# Changes in the Portfolio Offering

In 2009, the Caisse had five short-term strategic priorities, including the commitment to acting in a fiduciary spirit to provide long-term, risk-adjusted, liability-driven returns to its depositors. Among other efforts, this led to extensive changes to its specialized portfolio offering to better meet the needs of depositors in terms of choice, flexibility, transparency and asset-liability matching. Accordingly, the Caisse gradually launched its new portfolio offering during 2010. As was the case for the discussion stage preceding it, this deployment was carried out in close collaboration with the depositors.

## HIGHLIGHTS

**01** In 2010, the Caisse significantly changed its portfolio offering with depositors with the aim of simplifying it, making it more transparent and flexible for its clients.

**02** Assets with similar characteristics and risk-return profiles were grouped into the same portfolio.

**03** The benchmark indexes of some portfolios were changed to reflect modifications in their asset composition.

**04** Certain fixed income and equity portfolios are now indexed.

**05** In addition to its portfolio offering, the Caisse now proposes overlay strategies to its clients, offering customized hedging against certain risks.

## OBJECTIVES OF PORTFOLIO OFFERING CHANGES

The changes to the portfolio offering had the following objectives:

- Simplify the portfolios and increase transparency.
- Offer greater flexibility to depositors through new investment options and new currency, interest rate and inflation hedging strategies.
- Concentrate active management within asset classes where the Caisse possesses comparative advantages.
- Ensure specialized portfolio coherence and facilitate understanding of their risk-return profiles.
- Reduce and better manage the level of authorized leverage.

## SUMMARY OF CHANGES

Overall, the structure of the specialized portfolios was modified to achieve greater investment uniformity within each portfolio (see Table 5).

1. The 17 portfolios of the new offering were grouped into four broad risk-return profile categories: Fixed Income, Inflation-Sensitive Investments, Equity and Other Investments.
2. Assets that have similar characteristics and risk-return profiles were grouped into the same portfolio.
3. The investment policies of most portfolios were reviewed with an emphasis on investment universe, concentration limit and risk limit tightening, risk oversight including liquidity risk and leveraging, and transparency enhancement.
4. The benchmark indexes of some portfolios have been changed to reflect changes in their asset composition.

## Changes in the Portfolio Offering

- Value added objectives for the portfolios have been revised to reflect changes in their investment policy, their risk-return profile and the Caisse's comparative advantages.
- Certain fixed income and equity portfolios are now indexed. In the case of equity portfolios, depositors can choose between active management and indexation for equities outside Canada.
- A range of overlay strategies now complements the portfolio offering to provide each depositor with a customized hedge against currency risk. Other overlay strategies, which offer protection against inflation and interest rate risk, will be implemented gradually.

TABLE 5

### PORTFOLIO OFFERING

(as at December 31, 2010)

#### SPECIALIZED PORTFOLIOS<sup>1</sup>

<b>Fixed Income</b>	<i>Short Term Investments</i>
	Bonds
	<i>Long Term Bonds</i>
	Real Estate Debt
<b>Inflation-Sensitive Investments</b>	<i>Real Return Bonds</i>
	Infrastructure
	Real Estate
<b>Equity</b>	Canadian Equity
	Global Equity
	Québec International
	<i>U.S. Equity</i>
	<i>EAFE Equity</i>
	<i>Emerging Markets Equity</i>
	Private Equity
<b>Other Investments</b>	Hedge Funds
	Asset Allocation
	ABTN

1. The indexed portfolios are shown in italics.

### TIMELINE OF THE NEW OFFERING LAUNCH

Work on the launch of the new portfolio offering started at the end of 2009 with the establishment of an ambitious, three-phase action plan.

Throughout the entire process, the Caisse held numerous working meetings with depositors. At a late April seminar, for example, representatives of the Caisse – portfolio managers, risk management experts and investment group executives – presented to representatives of the depositors components of the new offering that would come into effect on June 1 and reviewed every investment policy with them.

Overall, the success of this large-scale operation is due to the mobilization of some 225 employees from various business units, who carried out this key element of the Caisse's roadmap for 2010.

#### JANUARY 1

- Creation of the ABTN portfolio.
- Closing of the Commodities portfolio.
- Adoption of index-based management for the Long Term Bonds and Real Return Bonds portfolios.

#### APRIL 1

- Creation of the Global Equity portfolio and gradual closing of the Québec International portfolio.
- Adoption of index-based management for the Short Term Investments, U.S. Equity, EAFE (Europe, Australasia, Far East) Equity and Emerging Markets Equity portfolios.
- Establishment of customized overlay strategies.

#### JULY 1

- Closing of the Investments and Infrastructures portfolio and transfer of the "Investments" portion to the Private Equity portfolio.
- Creation of the Infrastructure portfolio.
- Transfer of the "corporate lending" component of the Investments and Infrastructures portfolio to the Bonds portfolio and the distressed debt activities of the Bonds portfolio to the Private Equity portfolio.

# Overall Portfolio

## HIGHLIGHTS

**01** In 2010, the Caisse increased its equity exposure, primarily to private equity, and reduced its fixed income positions.

**02** As at December 31, 2010, 63.9% of depositors' total assets were invested in Canada.

**03** The 17 specialized portfolios are split into four broad risk-return profile categories.

**04** Eleven specialized portfolios are actively managed and six are indexed.

The Caisse invests the funds of its clients, the depositors. Its goal: provide them with long-term, risk-adjusted, liability-driven returns. To this end, it adopts a diversification strategy, using investment products in financial markets in Québec, Canada and abroad.

The Caisse offers depositors the ability to allocate their funds across various specialized portfolios, each consisting of securities from one asset class. An investment policy sets out the management philosophy and parameters for each specialized portfolio regarding, in particular, its investment universe, benchmark index, performance and value added objectives (in the case of an actively managed portfolio) – in addition to risk supervision with clearly defined concentration and risk limits.

## SPECIALIZED PORTFOLIOS

As at December 31, 2010, the Caisse offered its depositors 17 specialized portfolios, split into four broad risk-return profile categories.

### Fixed Income

The Fixed Income category reduces the portfolio's overall risk level and helps match depositors' assets to liabilities. It includes four portfolios:

- **Short Term Investments:** indexed portfolio.
- **Bonds:** this actively managed portfolio is concentrated in Canadian bonds (federal government, provincial governments, corporate) and includes corporate lending activities.
- **Long Term Bonds:** indexed portfolio.
- **Real Estate Debt:** this actively managed portfolio concentrates on high-quality Canadian mortgages.

### Inflation-Sensitive Investments

The Inflation-Sensitive Investments category provides exposure to investments whose income is generally indexed to inflation. This can partly hedge against the inflation risk associated with the liabilities of many depositors. It includes three portfolios:

- **Real Return Bonds:** indexed portfolio.
- **Infrastructure:** this actively managed portfolio includes the "Infrastructures" portion of the former Investments and Infrastructures portfolio. It concentrates on conservative investments with a high proportion of current income.
- **Real Estate:** actively managed portfolio where the maximum leverage level was lowered.

## Overall Portfolio

### Equity

The Equity category essentially enhances the expected returns of depositors. It includes seven portfolios:

- **Canadian Equity:** actively managed portfolio, based on an approach that seeks long-term capital growth.
- **Global Equity:** actively managed portfolio that primarily relies on a global sectoral approach and, in the case of emerging markets, a geographic allocation approach. External management is used, whenever necessary, to complement the expertise of Caisse managers. This portfolio will be gradually funded by the December 31, 2012 closure of the Québec International portfolio.
- **Québec International:** portfolio in the process of closing
- **U.S. Equity, EAFE Equity and Emerging Markets Equity:** indexed portfolios that are not hedged against currency risk.
- **Private Equity:** actively managed portfolio that includes the "Investments" component of the former Investments and Infrastructures portfolio.

### Other Investments

The Other Investments category includes three portfolios:

- **Hedge Fund:** actively managed portfolio, with a fund-of-funds strategy.
- **Asset Allocation:** actively managed portfolio that concentrates on tactical asset allocation and various strategies with the aim of protecting the overall portfolio against tail risks.
- **ABTN:** unfunded portfolio that consists of ABCPs, now called ABTNs (asset-backed term notes), established to ensure greater operational transparency.

### Overlay Strategies

In addition to these 17 portfolios, the Caisse has offered overlay strategies since April 1, 2010, allowing each depositor to customize a hedge against currency risk, among others. The Caisse enhanced its advisory services accordingly to better assist depositors in establishing their investment policies and choosing effective hedging strategies.

## ACTIVE MANAGEMENT AND INDEXATION

Active management continues to be the Caisse's main and preferred type of management. As a result, 11 portfolios representing about 81% of the net assets are actively managed and offer the possibility of generating added value. The other six portfolios are indexed, replicating benchmark indexes. These changes have allowed the Caisse to concentrate its efforts where it has comparative advantages, offering depositors the opportunity of choosing between actively managed or indexed international equity portfolios.

## GEOGRAPHIC DIVERSIFICATION

In addition to investing in Québec and Canada, the Caisse is active in global markets with investments in a variety of asset classes.

As at December 31, 2010, as Table 6 shows, the proportion of depositors' total assets invested outside Canada was essentially the same as at the end of 2009. Most of the Caisse's investments abroad were in industrialized countries. The United States continues to dominate with slightly less than half of these investments. The share of emerging markets continues to grow, considering the Caisse's strategy to take advantage of higher growth rates in these countries.

TABLE 6

### GEOGRAPHIC BREAKDOWN OF DEPOSITORS' TOTAL ASSETS<sup>1</sup>

(as at December 31 - in percentage)

	2010	2009
Canada	63.9	63.8
United States	16.6	17.2
Eurozone	5.9	6.8
United Kingdom	4.0	3.9
Japan	1.8	1.3
Emerging markets	4.7	4.2
Other	3.1	2.8
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

1. Based on the country of company or issuer headquarters, or for real estate, the geographical location of the assets.

## CURRENCY HEDGING

A large portion of the Caisse's international assets is protected against currency fluctuations through foreign exchange hedging instruments. In 2010, as in the past, the Caisse hedged the majority of foreign investments in its illiquid portfolios (Real Estate Debt, Infrastructure, Real Estate, Private Equity) against currency risk. However, effective April 1, 2010, it ceased hedging its liquid portfolios, such as publicly-traded securities portfolios. The Caisse subsequently established customized overlay strategies, which allow depositors to increase or reduce the currency exposure of their portfolios.

## BENCHMARK INDEXES

For each specialized portfolio, except for the Asset Allocation and ABTN portfolios, a benchmark index serves to compare the results of the managers against the corresponding market. In 2010, as changes were made to the portfolio offering, the Caisse adopted new benchmark indexes, ensuring that they are representative of various portfolio policies, by favouring the Québec component of certain indexes, for example.

The following are the main changes to the benchmark indexes of the specialized portfolios (also see Table 7).

### Fixed Income

- **Bonds:** replacement of the Provincial component with the Québec component of the DEX Universe Bond Index in order to favour a higher weighting of Québec bonds.
- **Long Term Bonds:** replacement of the Provincial component with the Québec component of the DEX Long Government Bond Index to reflect the portfolio's overweighting in Québec bonds.
- **Real Estate Debt:** replacement of the Barclays CMBS B Hedged Index with the Giliberto-Levy Hedged Index within the Real Estate Debt Index to reflect portfolio refocus on high-quality mortgages.

### Inflation-Sensitive Investments

- **Infrastructure:** establishment of an index composed of a basket of exchange-traded securities, hedged and representative of the mandate of this new portfolio.
- **Real Estate:** replacement of the Aon – Real Estate Index with the Aon Hewitt – Real Estate (Adjusted) Index, to reflect leverage more representative of the portfolio and adjusted for management and administration fees.

### Equity

- **Global Equity:** selection of the unhedged MSCI ACWI (All Country World Index), representative of this new portfolio's mandate.
- **U.S. Equity, EAFE Equity:** selection of the S&P 500 Unhedged and MSCI EAFE Unhedged, representative of the respective mandates of these new portfolios.
- **Private Equity:** change in the composition of the index to ensure it is more representative of private equity and the portfolio's new mandate following the integration of the "Investments" part of the former Investments and Infrastructures portfolio.

Table 7 presents the evolution of the benchmark indexes over five years.

TABLE 7

## EVOLUTION OF THE BENCHMARK INDEXES OVER 5 YEARS

(as at December 31, 2010)

SPECIALIZED PORTFOLIO	BENCHMARK INDEX
<b>SHORT TERM INVESTMENTS</b> (Created July 1, 1998)	DEX 91 Day T-Bill
<b>BONDS</b> (Created October 1, 1996)	DEX Universe Bond (Adjusted) since July 1, 2010. Formerly DEX Universe Bond.
<b>LONG TERM BONDS</b> (Created April 1, 2005)	DEX Long Term Government Bond (Adjusted) since July 1, 2010. Formerly DEX Long Term Government Bond.
<b>REAL ESTATE DEBT</b> (Created April 1, 1995)	Real Estate Debt (index consists of 90% DEX Universe Bond and 10% Giliberto-Levy Hedged) since January 1, 2010. Formerly 90% DEX Universe Bond and 10% Barclays CMBS B Hedged.
<b>REAL RETURN BONDS</b> (Created January 1, 2004)	DEX Real Return Bond
<b>INFRASTRUCTURE</b> (Created July 1, 2010)	Infrastructures (index consists of a basket of infrastructure-related public securities, hedged)
<b>REAL ESTATE</b> (Created October 1, 1985)	Aon Hewitt – Real Estate (Adjusted) since January 1, 2010. Formerly Aon – Real Estate.
<b>CANADIAN EQUITY</b> (Created July 1, 1995)	S&P/TSX Capped
<b>GLOBAL EQUITY</b> (Created April 1, 2010)	MSCI ACWI Unhedged
<b>QUÉBEC INTERNATIONAL</b> (Created July 1, 1999)	Québec International (index consists of 80% DEX Québec Bond and 20% DEX 91 Day T-Bill, plus a basket of equity futures.)
<b>U.S. EQUITY</b> (Created April 1, 2010)	S&P 500 Unhedged
<b>EAFE EQUITY</b> (Created April 1, 2010)	MSCI EAFE Unhedged
<b>EMERGING MARKETS EQUITY</b> (Created January 1, 1995)	MSCI EM Unhedged
<b>PRIVATE EQUITY</b> (Created July 1, 2003)	Private Equity (index consists of 70% State Street Private Equity Index Adjusted and 30% MSCI World, Hedged, effective since July 1, 2010. Formerly 60% S&P 500 Hedged and 40% MSCI EAFE Hedged from October 1, 2006 to June 30, 2010, S&P 600 Adjusted previously)
<b>HEDGE FUND</b> (Created April 1, 2003)	Dow Jones Credit Suisse Hedge Fund Index Adjusted (Hedged) since July 1 2007. Formerly SC 91-Day Canadian T-Bill from July 1, 2006 to June 30, 2007, S&P Hedge Fund Index previously.
<b>CLOSED IN 2010</b>	
<b>COMMODITIES</b> (Closed January 1, 2010)	Index based 80% on the Barclays U.S. Government Inflation-Linked Bond 1-10 Year Total Return Index and 20% on the Merrill Lynch 3-month U.S. Treasury Bill, plus the unhedged Dow Jones-AIG Commodity Excess Return Index.
<b>U.S. EQUITY HEDGED</b> (Closed March 31, 2010)	S&P 500 Hedged
<b>U.S. EQUITY UNHEDGED</b> (Closed March 31, 2010)	S&P 500 Unhedged
<b>FOREIGN EQUITY HEDGED</b> (Closed March 31, 2010)	MSCI EAFE Hedged
<b>FOREIGN EQUITY UNHEDGED</b> (Closed March 31, 2010)	MSCI EAFE Unhedged
<b>INVESTMENTS AND INFRASTRUCTURES</b> (Closed June 30, 2010)	Investments and Infrastructures (index consisted of 50% S&P/TSX Capped, 25 % S&P 500 Hedged and 25% MSCI EAFE Hedged since October 1, 2006, S&P/TSX adjusted previously.)

## BENCHMARK PORTFOLIO

The weighted average of the asset allocation established by the depositors' investment policies makes it possible to determine the composition of the Caisse's benchmark portfolio. As at December 31, 2010, the overall portfolio's asset allocation conformed to the parameters of the benchmark portfolio. During the year, the Caisse increased its equity exposure, mainly to private equity, and reduced its fixed income positions (see Table 8).

## Currency exposure

Effective April 1, 2010, overlay strategies allowed the depositors to vary their currency exposure according to their respective portfolios and risk tolerance. As at December 31, 2010, the benchmark portfolio included 5.6% U.S. dollar exposure and 7.5% exposure to the basket of EAFE currencies.

TABLE 8

COMPOSITION OF THE BENCHMARK PORTFOLIO  
AND EVOLUTION OF THE OVERALL PORTFOLIO

(percentage of depositors' net assets)

	Benchmark portfolio as at December 31, 2010 <sup>1</sup>			Caisse's overall portfolio	
	Lower limit %	Benchmark portfolio %	Upper limit %	as at December 31, 2010 %	as at December 31, 2009 %
<b>Fixed Income</b>					
Short Term Investments	0.2	1.2	9.1	2.5	2.2
Bonds	21.4	26.5	36.1	26.4	28.7
Long Term Bonds	1.8	2.4	4.4	2.4	2.4
Real Estate Debt	2.5	6.5	10.0	5.6	6.9
<b>Total</b>		36.6		36.9	40.2
<b>Inflation-Sensitive Investments</b>					
Real Return Bonds	0.1	0.6	2.5	0.6	0.5
Infrastructure <sup>2</sup>	0.7	3.3	6.9	2.9	4.1
Real Estate	6.3	10.1	14.6	11.0	10.9
<b>Total</b>		14.0		14.5	15.5
<b>Equity</b>					
Canadian Equity	7.4	12.9	18.4	12.7	13.0
Global Equity	1.1	3.4	5.7	3.9	N/A
Québec International	2.2	6.4	9.4	5.6	9.8
U.S. Equity	0.7	4.0	8.6	3.8	3.6
EAFE Equity	1.5	6.5	10.3	6.4	5.2
Emerging Markets Equity	0.6	3.8	7.0	3.8	3.8
Private Equity	6.5	9.9	13.2	11.5	8.6
<b>Total</b>		46.9		47.7	44.0
<b>Other Investments</b>					
Hedge Funds	0.1	2.5	4.6	2.2	2.9
Asset Allocation	0.0	0.0	1.0	0.4	0.4
ABTN	N/A	N/A	N/A	(1.7)	(3.9)
Commodities <sup>3</sup>	N/A	N/A	N/A	0.0	0.9
<b>Total</b>		100.0		100.0	100.0

1. The benchmark portfolio and its upper and lower limits are the result of the weighted average of the depositors' benchmark portfolios.

2. The percentage of the overall portfolio in 2009 corresponds to the Investments and Infrastructures portfolio.

3. The Commodities portfolio was closed on January 1, 2010.

# Analysis of Overall Performance

In 2010, the Caisse's management teams held their own in an environment marked by turbulence, Europe's sovereign debt crisis, fears of a slowing U.S. economy and, at the end of year, rising stock markets due to new stimulus measures in the U.S. and a sharp increase in corporate profits. They were able to refocus the Caisse on its core businesses and select high-quality assets, while managing their portfolios rigorously.

The quality of its portfolio securities and the expertise of its teams enabled the Caisse to benefit from the recovery of less liquid markets. This rebound, due mainly to a gradual reopening of credit markets and the availability of investor capital, was stronger for high-quality assets – not only securities in less liquid portfolios, but also corporate debt and commercial mortgages.

## HIGHLIGHTS

**01** The three major asset classes of the Caisse's portfolio – Fixed Income, Inflation-Sensitive Investments and Equity – contributed to the overall performance and the net investment results in 2010.

**02** Nine of the 11 actively managed specialized portfolios outperformed their benchmark index or added value.

**03** The hedge against foreign exchange risk minimized the negative impact of the stronger Canadian dollar.

**04** Annual returns of the seven main depositors ranged between 13.2% and 14.3%.

As at December 31, 2010, the Caisse's overall portfolio saw a 13.6% weighted average return on depositors' funds and net investment results amounted to \$17.7 billion. The three major asset classes of the portfolio contributed positively to these results (see Table 9):

- Fixed Income posted a 9.7% return and \$4.9 billion in net investment results.
- Inflation-Sensitive Investments generated a 16.3% return and \$3.1 billion in net investment results.
- Equity returned 14.6% and \$9.2 billion in net investment results.

At the end of 2010, the Caisse's overall portfolio outperformed the benchmark portfolio by 415 b.p. (4.15%). In addition, nine of the 11 actively managed portfolios beat their benchmark index or added value.

## CURRENCY EXPOSURE

As at December 31, 2010, the proportion of depositors' total assets outside Canada and, in turn, exposed to currency fluctuations amounted to more than 90%. A significant portion of the risk of the exposure to foreign currencies was hedged by currency derivatives. The currency derivatives are designated to adjust the level of the currency hedge.

For 2010, foreign currency depreciated against the Canadian dollar: 5.2% for the U.S. dollar and 2.6% for the EAFE basket of currencies. Hedging most of the currency exposure risk reduced the negative impact of the stronger Canadian dollar by approximately two-thirds.

TABLE 9

## NET ASSETS AND RETURNS IN RELATION TO BENCHMARK INDEXES

(for periods ended December 31, 2010)

Asset classes	1 year				5 years			
			Net investment results <sup>1</sup>				Net investment results	
	Net assets	Return		Spread <sup>2</sup>	Return		Spread	
	\$B	%	\$M	(b.p.)	%	\$M	(b.p.)	
Fixed Income	55.6	9.7	4,945	271	4.0	10,473	(88)	
Inflation-Sensitive Investments	22.0	16.3	3,096	558	3.1	3,681	(28)	
Equity	12.4	14.6	9,190	453	9.9	10,317	173	
Hedge Funds	3.3	6.3	200	11	9.1	204	79	
ABTN <sup>3,4</sup>	(2.6)	N/A	509	N/A	N/A	N/A	N/A	
Asset Alloc <sup>5</sup>	0.6	N/A	(77)	N/A	N/A	(1,100)	N/A	
Total <sup>5</sup>	151.7	13.6	17,731	416	7.0	16,385	(123)	

1. The net investment results include the impact of operating expenses and other fees.

2. Compared to the benchmark indexes.

3. The ABTN includes the net value of its investments and equity accounts for the negative net assets.

4. Since December 31, 2010, the ABTN provision, combined with fees and associated interest income, totaled \$6.2 billion. The impact on value added totaled \$7.6 billion over the five years.

5. Net assets and net investment results include the customized Overlay Strategies of the depositors and cash activities.

## Analysis of Overall Performance

### FIVE-YEAR RETURN

For the five years ended December 31, 2010, the Caisse generated an annualized return of 2.6%. This performance is largely due to the performance of 2008, as shown in Table 10. In fact, the average of annual returns for 2006, 2007, 2008 and 2009 is 0.0%.

This result of 2.6% for the five-year period underperforms the benchmark index by 0.6% (0.0%). The deviation of the under-performance is due to AER results. The remainder mainly stems from the Real Estate Debt and Real Estate portfolios. During this period, the Short Term Investments, Bonds, Canadian Equity, Private Equity and Hedge Funds portfolios had a particularly positive impact from a value added standpoint.

### DEPOSITORS' INDIVIDUAL RETURNS

The overall return is based on the weighted average return on depositors' funds. Accordingly, depositors obtain returns based on their investment policy, which determines their asset allocation for each specialized portfolio.

In 2010, the return for the short-term depositors averaged 0.7% to 0.9%. For the past five years, these depositors have obtained annualized returns ranging from 2.2% to 3.8%.

### RETURNS BY SPECIALIZED PORTFOLIO

Table 11 shows the returns of the specialized portfolios relative to their benchmark index for the one-year and five-year periods ending December 31, 2010.

TABLE 10

### CAISSE RETURNS

(for periods ended December 31 – in percentage)

	Caisse's overall return <sup>1</sup>
2010	13.0
2009	10.0
2008	(25.0)
2007	5.8
2006	14.6
5-year average (2006-2010)	2.6

1. Weighted average return on depositors' funds.  
2. The return percentage is annualized.

TABLE 10

## SPECIALIZED PORTFOLIO RETURNS IN RELATION TO BENCHMARK INDEXES

(for periods ended December 31, 2010 – percentage (prices other than notated))

Specialized portfolio	2010 Index <sup>1</sup>	1 year			5 years		
		Return <sup>2</sup> %	Index <sup>3</sup> %	Spread (b.p.)	Return <sup>2</sup> %	Index <sup>3</sup> %	Spread (b.p.)
<b>Fixed Income</b>							
Short-Term Investments <sup>4</sup>	DEZ 91 Day T-Bill	9.7	9.9	12	9.9	9.9	29
Bonds	DEZ Universe Bond (Adjusted)	8.8	8.8	189	5.5	5.5	29
Long-Term Bonds <sup>5</sup>	DEZ Long-Term Government Bond (Adjusted)	12.9	12.9	(9)	6.4	6.4	(39)
Real Estate Debt <sup>6</sup>	Real Estate Debt	17.1	7.1	999	(5.5)	4.2	(619)
<b>Total</b>		9.7	7.9	271	4.9	4.9	(99)
<b>Alternative Securities Investments</b>							
Real Return Bonds <sup>7</sup>	DEZ Real Return Bond	11.1	11.1	9	4.6	4.7	(11)
Infrastructure <sup>8</sup>	Infrastructure	25.4	11.9	1,419	2.7	3.6	(26)
Real Estate <sup>9</sup>	Aon Hewitt – Real Estate (Adjusted)	13.4	11.6	184	4.0	7.6	(365)
<b>Total</b>		16.3	10.7	556	3.1	5.6	(252)
<b>Equity</b>							
Canadian Equity	S&P/TSX Capped	15.7	17.6	(190)	8.0	6.5	150
Global Equity <sup>4</sup>	MSCI ACWI (Unhedged)	7.3	7.0	29	N/A	N/A	N/A
Québec International	Québec International	14.0	13.7	34	0.8	1.2	(34)
U.S. Equity <sup>10</sup>	S&P 500 (Unhedged)	9.8	9.6	23	(2.2)	(0.6)	(164)
EAFE Equity <sup>10</sup>	MSCI EAFE (Unhedged)	4.1	3.9	19	(1.0)	(0.8)	(12)
Emerging Markets Equity <sup>7</sup>	MSCI EM (Unhedged)	12.0	12.7	(63)	7.6	9.2	(156)
Private Equity	Private Equity	26.7	2.0	2,474	7.9	(2.2)	1,010
<b>Total</b>		14.6	10.0	453	3.9	2.2	173
<b>Other Investments</b>							
Hedge Funds	Dow Jones Credit Suisse Hedge Fund Index (Adjusted Hedged)	6.3	6.2	11	2.1	1.4	79
Asset Allocation <sup>1</sup>		\$177MM	N/A	N/A	\$177MM	N/A	N/A
ABTN <sup>2</sup>		\$509 M	N/A	N/A	N/A	N/A	N/A
<b>Weighted Average Return on deposits funds</b>		13.5	8.5	415	3.5	4.0	(112)

1. These portfolios have been indexed since April 1, 2010.

2. These portfolios have been indexed since January 1, 2010.

3. This line includes the Infrastructure and Infrastructure Funds portfolios from January 1, 2006, to June 30, 2010, and the Infrastructure portfolio since July 1, 2010.

4. This portfolio was launched on April 1, 2010. The returns are for the period of April 1 to December 31, 2010.

5. This line includes the U.S. Equity (Unhedged) and U.S. Equity (Unhedged) portfolios from January 1, 2006, to March 31, 2010, and the new U.S. Equity portfolio since April 1, 2010.

6. This line includes the Foreign Equity (Unhedged) and Foreign Equity (Unhedged) portfolios from January 1, 2006, to March 31, 2010, and the new Europe, Australasia &amp; Far East (EAFE) Equity portfolio since April 1, 2010.

7. The net investment results in dollars are net of operating expenses and other fees.

8. Since December 2007, the ABTN provision, combined with fees and associated interest arrears, totaled –\$5.2 billion. The impact on value added totaled 37 b.p. in 2010 and –82 b.p. over five years.

9. The description of the indexes is presented in table 7, p. 28.

10. The return percentages are annualized and the net investment results in dollars are cumulative.

# Analysis of Performance by Asset Class

## FIXED INCOME

As at December 31, 2010, the Fixed Income class consisted of four portfolios. The Bonds and Real Estate Debt portfolios, with total net assets of \$48.6 billion, are actively managed. The Short Term Investments and Long Term Bonds portfolios, with total net assets of \$7.0 billion, are indexed.

### HIGHLIGHTS

**01** The overall return of the Fixed Income class was 9.7%, 271 b.p. (2.71%) above the benchmark index.

**02** The Fixed Income class had total net assets of \$55.6 billion as at December 31, 2010.

**03** The Bonds portfolio, actively managed, achieved a return of 8.4%, 160 b.p. (1.60%) above its benchmark index.

**04** The Real Estate portfolio, actively managed, delivered a return of 17.1%, 995 b.p. (9.95%) above its benchmark index. This includes a current yield of 7.2%.

### MARKET ENVIRONMENT

Highly prized by foreign investors, the Canadian bond market performed well in 2010, supported particularly by a favourable fiscal situation and strong dollar. Although the Bank of Canada raised its key rate by 25 b.p. to 2.5% in three times, medium- and long-term government of Canada bond rates declined before rising again in the fourth quarter.

In 2010, global bond markets were initially affected by concerns about the creditworthiness of certain European countries and fears of an economic slowdown in the United States. Support measures by the authorities (International Monetary Fund, European Union and European Central Bank) finally calmed markets in Europe, leading to a gradual narrowing of credit spreads in the fourth quarter. In the U.S., a second wave of monetary easing in the fall was not enough to maintain the downward trend in rates that began in the second quarter. A U.S. economic recovery, coupled with continued tax cuts, was behind a large part of the rate hike in the fourth quarter.

Given an environment of low interest rates, a rebound in quality commercial property market valuations and a renewed appetite for risk, the real estate debt market saw a substantial improvement in liquidity. In addition, mortgage rate spreads contracted significantly, enabling the market to end the year on a good note.

## PORTFOLIO RETURNS

For 2010, the overall performance of the Fixed Income class was 9.7%, 271 b.p. (2.71%) above the benchmark index (see Table 12).

### Short Term Investments

The Short Term Investments portfolio produced a return of 0.7%, 12 b.p. (0.12%) above its benchmark index. This performance is due to an environment of very low short-term rates.

### Bonds

The Bonds portfolio returned 8.4%, 160 b.p. (1.60%) above its benchmark index.

Lower medium- and long-term rates during the year positively contributed to portfolio returns. About three quarters of the added value is due to insightful corporate bond selection. The other quarter comes primarily from provincial and sovereign bond selection.

Table 13 presents the returns of the DEX Bond Indexes, by maturity and issuer. In 2010, the returns were largely influenced by the decline in medium- and long-term rates. In 2009, they were mainly linked to the decrease in rate spreads between government and corporate bonds, which explains the bigger spreads between subindex returns for 2009.

TABLE 12

## SPECIALIZED PORTFOLIO RETURNS – FIXED INCOME

(for periods ended December 31, 2010)

	1 year				5 years		
	Depositors' net assets \$B	Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)	Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)
Short Term Investments <sup>3</sup>	3.4	0.7	0.5	12	2.9	2.6	29
Bonds	40.0	8.4	6.8	160	5.5	5.3	23
Long Term Bonds <sup>4</sup>	3.6	12.3	12.3	(2)	5.4	5.5	(12)
Real Estate Debt	8.6	17.1	7.1	995	(1.5)	4.2	(570)
<b>Total</b>	<b>55.6</b>	<b>9.7</b>	<b>7.0</b>	<b>271</b>	<b>4.0</b>	<b>4.9</b>	<b>(89)</b>

1. The description of the indexes is presented in Table 7, p. 28.

2. Compared to the benchmark indexes.

3. This portfolio has been indexed since April 1, 2010.

4. This portfolio has been indexed since January 1, 2010.

TABLE 13

## DEX BOND INDEXES RETURNS

(in percentage)

DEX Bond Indexes	2010				2009			
	Short Term	Medium Term	Long Term	Total	Short Term	Medium Term	Long Term	Total
Federal	3.19	7.17	12.24	5.39	1.46	(1.60)	(3.82)	(0.21)
Provincial	3.75	7.83	11.84	8.56	3.85	5.45	5.01	4.72
Québec	3.69	7.89	11.82	8.91	3.70	5.92	5.79	5.40
Corporate	4.31	8.24	14.23	7.34	10.97	21.30	25.87	16.26
<b>Universe</b>	<b>3.56</b>	<b>7.80</b>	<b>12.52</b>	<b>6.74</b>	<b>4.54</b>	<b>7.54</b>	<b>5.49</b>	<b>5.41</b>

## Analysis of Performance by Asset Class

### Long Term Bonds

The Long Term Bonds portfolio reported a return of 12.3%, practically identical to its index. This performance is mainly explained by the increases in value linked to falling long-term rates.

### Real Estate Debt

The Real Estate Debt portfolio delivered a return of 17.1%, 995 b.p. (9.95%) above its benchmark index. This includes a current yield of 7.2%.

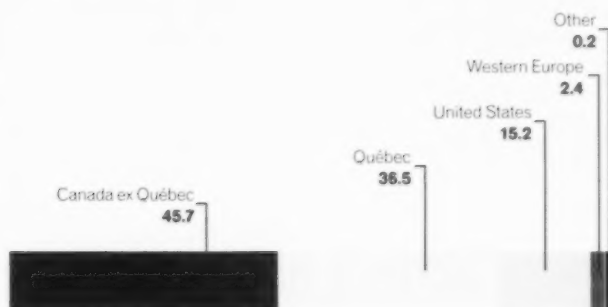
This 17.1% return is the result, among others, of falling mortgage rates in Canada, including spread tightening. In addition, the recovery of the commercial real estate market outside Canada (office buildings and retail) allowed a sale of assets as part of the portfolio refocusing announced in 2009, which resulted in a reduction of the U.S. investment weight from 26.0% as at December 31, 2009 to 15.2% as at December 31, 2010.

As at December 31, 2010, investments in Canada (Québec and Canada ex Québec) accounted for 82.2% of the portfolio's fair value, compared to 67.0% as at December 31, 2009, which reflects the portfolio's objective of concentrating on high-quality Canadian mortgages (see Figure 14).

FIGURE 14

### GEOGRAPHIC BREAKDOWN – REAL ESTATE DEBT

(in percentage of fair value as at December 31, 2010)



As at December 31, 2010, investments in the office building sector represented the largest portion of the portfolio (see Figure 15).

FIGURE 15

### SECTOR BREAKDOWN – REAL ESTATE DEBT

(in percentage of fair value as at December 31, 2010)



## INFLATION-SENSITIVE INVESTMENTS

As at December 31, 2010, the Inflation-Sensitive Investments class consisted of three portfolios. The Infrastructure and Real Estate portfolios, with total net assets of \$21.1 billion, are actively managed. The Real Return Bonds portfolio, with total assets of \$0.9 billion, is indexed.

### HIGHLIGHTS

**01** The overall performance of the Inflation-Sensitive Investments class was 16.3%, 558 b.p. (5.58%) above the benchmark index.

**02** This class had total net assets of \$22.0 billion as at December 31, 2010.

**03** The 25.4% return on investments in the Infrastructure portfolio is due to the solid operational performance of its assets.

**04** The Real Estate portfolio realized a return of 13.4%, 184 b.p. (1.84%) above its index.

### MARKET ENVIRONMENT

From December 2009 to December 2010, the inflation rate in Canada rose to 2.4%, while the Bank of Canada's long-term target rate was 2%. Inflation-sensitive asset classes still saw considerable returns – due to a rebound in activity in illiquid markets, such as real estate and infrastructure, and a backdrop of falling medium- and long-term rates that benefited real return bonds.

In the second and third quarter, bond markets saw interest rates drop, followed by upward movement in the fourth quarter. This was also the case for the real return bond market. However, the increase in real interest rates was slightly lower than the nominal rate hike due to upward inflation expectations for the period.

The gradual reopening of credit markets translated into a rebound of activity in the infrastructure sector during 2010. These elements led to an increase in major transactions in the second semester. Furthermore, the money accumulated by infrastructure funds reached \$19 billion, compared to \$10.7 billion in 2009. In addition, the sector's resilience during the last economic cycle encouraged institutional investors to increase their infrastructure weighting in their portfolios. The sector, in particular, presents long-term investment opportunities, both in emerging markets, where infrastructure needs are immense, and developed countries, where aging infrastructure must be replaced.

In 2010, low interest rates and increased access to quality asset financing also led to a resurgence of activity in real estate markets. The availability of capital and the scarcity of products on the market led to a compression of capitalization rates and, in turn, higher prices for the best assets in Canada and the United States. In contrast, the sovereign debt crisis and fiscal austerity measures in Europe undermined investor confidence in the region's growth potential, which induced a shift of investments, particularly to the United States. On the emerging market front, their growing popularity with institutional investors also exerted upward pressure on prices.

## Analysis of Performance by Asset Class

### RETURNS ON THE PORTFOLIOS

For 2010, the overall performance of the Inflation-Sensitive Investments class was 16.3%, 558 b.p. (5.58%) above the benchmark index (see Table 16).

#### Real Return Bonds

The Real Return Bonds portfolio posted a return of 11.1%, practically identical to its benchmark index. This performance is essentially due to the decline in real long-term interest rates.

#### Infrastructure

In the first half of 2010, infrastructure investments were grouped in the Investments and Infrastructures portfolio. In the second half, these investments were integrated into the new Infrastructure portfolio.

After this change, the portfolio management team was able to better focus its efforts. It targeted two major transactions: a \$258 million investment in South East Water, a British water distribution company, and a \$227 million investment to acquire the Laurentides Investissements S.A.S. stake in Noverco, an investment company that holds 100% of Gaz Métro Inc.

For the year, the combined return of these portfolios stood at 25.4%, 1,413 b.p. (14.13%) above the benchmark index. This return is due to the good operational performance of the assets in the portfolio, particularly the airport service investments, including BAA, and energy assets, such as Enbridge Energy Partners, Interconnector UK and Noverco (Gaz Métro). The performance also stems from a general reduction in discount rates.

The portfolio assets possess strong fundamentals that improved during the year and saw an increase in their EBITDA (earnings before interest, taxes, depreciation and amortization).

As shown in Figure 17, investments in Western Europe accounted for the largest share of the portfolio as at December 31, 2010. The Caisse's managers are very familiar with this market, where private infrastructure holdings have been developed over many years, and rely on the support of excellent partners to invest there.

FIGURE 17

### GEOGRAPHIC BREAKDOWN – INFRASTRUCTURE

(in percentage of fair value as at December 31, 2010)

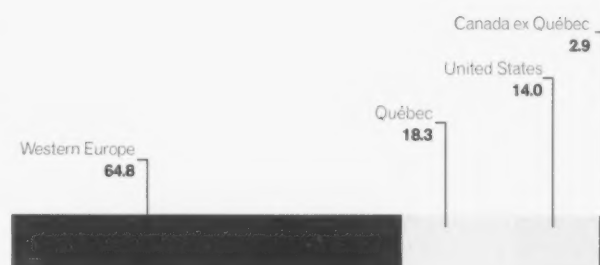


TABLE 16

### SPECIALIZED PORTFOLIO RETURNS – INFLATION-SENSITIVE INVESTMENTS

(for periods ended December 31, 2010)

	Depositors' net assets \$B	1 year			5 years		
		Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)	Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)
Real Return Bonds <sup>3</sup>	0.9	11.1	11.1	3	4.6	4.7	(11)
Infrastructure <sup>4</sup>	4.3	25.4	11.3	1,413	2.7	3.0	(25)
Real Estate	15.8	13.4	11.6	184	4.0	7.6	(365)
<b>Total</b>	<b>22.0</b>	<b>16.3</b>	<b>10.7</b>	<b>558</b>	<b>3.1</b>	<b>5.6</b>	<b>(252)</b>

1. The description of the indexes is presented in Table 7, p. 28.

2. Compared to the benchmark indexes.

3. This portfolio has been indexed since January 1, 2010.

4. This line combines the Investments and Infrastructures portfolio from January 1, 2006, to June 30, 2010, and the Infrastructure portfolio since July 1, 2010.

### Real Estate

This portfolio's return was 13.4%, 184 b.p. (1.84%) above its benchmark index.

In 2010, the Real Estate portfolio benefited from a gradual improvement of the global climate for quality assets. Price increases in the retail and office building sectors in Canada and the United States, combined with a stabilization of fundamentals in the office building benchmark markets in the United States (New York, Washington and Boston), explain most of the portfolio's performance.

In Europe, higher office building prices in London and Paris, driven by the increased demand of foreign investors, also contributed positively to the portfolio's return.

As at December 31, 2010, investments in Canada accounted for 47.3% of the portfolio's fair value and investments in the United States represented 23.8%, compared to 42.9% and 24.6%, respectively, as at December 31, 2009 (see Figure 18).

FIGURE 18

### GEOGRAPHIC BREAKDOWN – REAL ESTATE

(in percentage of fair value as at December 31, 2010)

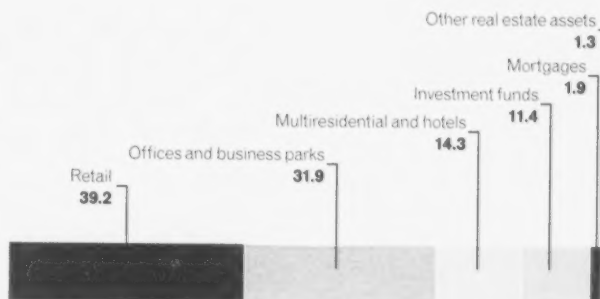


As at December 31, 2010, the retail sector represented the largest weight in the portfolio, followed by office buildings and business parks (see Figure 19).

FIGURE 19

### SECTOR BREAKDOWN – REAL ESTATE

(in percentage of fair value as at December 31, 2010)



## Analysis of Performance by Asset Class

### EQUITY

The Equity class consisted of seven portfolios as at December 31, 2010. The Canadian Equity, Global Equity and Québec International portfolios, with total net assets of \$33.6 billion, are actively managed. The U.S. Equity, EAFE Equity and Emerging Markets Equity portfolios, with total net assets of \$21.3 billion, are indexed. Finally, the Private Equity portfolio, with net assets of \$17.5 billion, is actively managed.

#### HIGHLIGHTS

**01** The Equity class reported an overall return of 14.6%, 453 b.p. (4.53%) above the benchmark index. This class held total net assets of \$72.4 billion as at December 31, 2010.

**02** The Canadian Equity portfolio produced a return of 15.7%, 190 b.p. (1.90%) below its benchmark index. Over five years, its annualized return outperformed the index by 150 b.p. (1.50%).

**03** The new Global Equity portfolio posted a return of 7.3%, slightly higher than its index, for the period from April 1 to December 31, 2010.

**04** The 26.7% return on the Private Equity portfolio is due largely to the improved operational performance of companies in the portfolio, leading to their increased earnings.

#### MARKET ENVIRONMENT

After the strong rally, which began in March 2009, major stock markets had a very volatile 2010, which finally ended on a good note. Overall, returns were, on average, 10% (see Figure 21). This is due to accommodative monetary policies throughout the world, steady emerging market demand and higher corporate profits, including those of companies constituting the S&P 500, whose profit growth approached 45%.

From January to August, uncertainty surrounding the eurozone and its potential impact on the global economy stalled markets, keeping indexes in fairly neutral territory. The temporary resolution of this crisis, a second round of monetary easing in the U.S. and better economic growth and employment numbers eventually pushed stock markets up in the last four months of the year.

On the private equity front, the year was marked by a gradual recovery in mergers and acquisitions, with most of the increase in the second half. Transactions totaled close to US\$2 trillion worldwide, an increase of 23% compared to 2009. The gradual reopening of financing markets led to a resumption of trading and contributed to the revaluation of securities. The high-yield debt market was particularly strong, with issues totaling US\$450 billion for the year. In this environment, private equity firms saw their portfolios stabilize and were more active in the market. About 1,300 transactions (including approximately 300 valued over US\$50 million), totaling US\$200 billion were completed during the year.

## RETURNS ON THE PORTFOLIOS

For 2010, the Equity class reported an overall return of 14.6%, 453 b.p. (4.53%) above the benchmark index (see Table 20).

### Canadian Equity

In 2010, the Canadian market posted the highest return of the G7 countries. The Caisse allocates the largest portion of its stock market investments in this market.

The Canadian Equity portfolio generated a return of 15.7%, 190 b.p. (1.90%) below its benchmark index. The portfolio's absolute return is mainly due to high exposure to the energy and materials sectors. Relative to its benchmark index, the Canadian Equity portfolio maintains a greater exposure to large-capitalization companies with compelling fundamentals. In an environment where small companies outperformed their large counterparts, this stock selection primarily explains the underperformance of this portfolio relative to its benchmark index. However, the absolute return strategies contributed positively to portfolio performance.

For the five-year period ended December 31, 2010, the Canadian Equity portfolio posted an annualized return of 8.0%, 150 b.p. (1.50%) above the benchmark index.

### Global Equity

This new portfolio, created on April 1, 2010, saw a 7.3% return, 29 b.p. (0.29%) above its benchmark index. This performance was mainly due to the active management activities at the New York office, namely through insightful stock selection in energy, industrials and consumer goods, and via absolute return strategies.

### Québec International

The Québec International portfolio posted a 14.0% return, outperforming its benchmark index by 34 b.p. (0.34%). International stock market performance and the high yield of Québec bonds led to the portfolio's absolute return. The value added essentially comes from an active management approach to the stock markets.

TABLE 20

## SPECIALIZED PORTFOLIO RETURNS – EQUITY

(for periods ended December 31, 2010)

	1 year				5 years		
	Depositors' net assets \$B	Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)	Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)
Canadian Equity	19.3	15.7	17.6	(190)	8.0	6.5	150
Global Equity <sup>3</sup>	5.9	7.3	7.0	29	N/A	N/A	N/A
Québec International	8.4	14.0	13.7	34	0.8	1.2	(34)
U.S. Equity <sup>4,5</sup>	5.8	9.8	9.6	23	(2.2)	(0.6)	(164)
EAFE Equity <sup>4,6</sup>	9.7	4.1	3.9	19	(1.0)	(0.8)	(12)
Emerging Markets Equity <sup>4</sup>	5.8	12.0	12.7	(63)	7.6	9.2	(156)
Private Equity	17.5	26.7	2.0	2,474	7.9	(2.2)	1,010
<b>Total</b>	<b>72.4</b>	<b>14.6</b>	<b>10.0</b>	<b>453</b>	<b>3.9</b>	<b>2.2</b>	<b>173</b>

1. The description of the indexes is presented at Table 7, p. 28.

2. Compared to the benchmark indexes.

3. This portfolio was launched on April 1, 2010. The return is for the period from April 1 to December 31, 2010.

4. These portfolios have been indexed since April 1, 2010.

5. This line combines the U.S. Equity (hedged and unhedged) portfolios from January 1, 2006, to March 31, 2010, and the new U.S. Equity portfolio since April 1, 2010.

6. This line combines the Foreign Equity (hedged and unhedged) portfolios from January 1, 2006, to March 31, 2010, and the new Europe, Australasia and Far East (EAFE) portfolio since April 1, 2010.

## Analysis of Performance by Asset Class

### U.S. Equity

The portfolios generated a 9.8% return, 23 b.p. (0.23%) above the benchmark index. This added value is due to the fact that the U.S. Equity portfolio was actively managed until March 31, 2010. Since April 1, the investment strategy for this market has been changed – the new U.S. Equity portfolio is now indexed. The active management activities were transferred to the Global Equity portfolio.

### EAFE Equity

The portfolios produced a 4.1% return, 19 b.p. (0.19%) above the benchmark index. This added value is due to the fact that the Foreign Equity portfolio was actively managed until March 31, 2010. Since April 1, the strategy for this market has been changed and the EAFE Equity portfolio is indexed. The active management activities were transferred to the Global Equity portfolio.

Concerns over the state of public finances and the economic outlook of certain European Union members weighed heavily on portfolio performance.

### Emerging Markets Equity

The Emerging Markets Equity portfolio posted a 12.0% return, 63 b.p. (0.63%) below its benchmark index. This underperformance is in part due to the termination of external management mandates in the first quarter.

Since April 1, 2010, this portfolio has been indexed. The active management activities were transferred to the Global Equity portfolio.

Strong economic growth in these markets positively contributed to portfolio returns. However, performance varied considerably between countries.

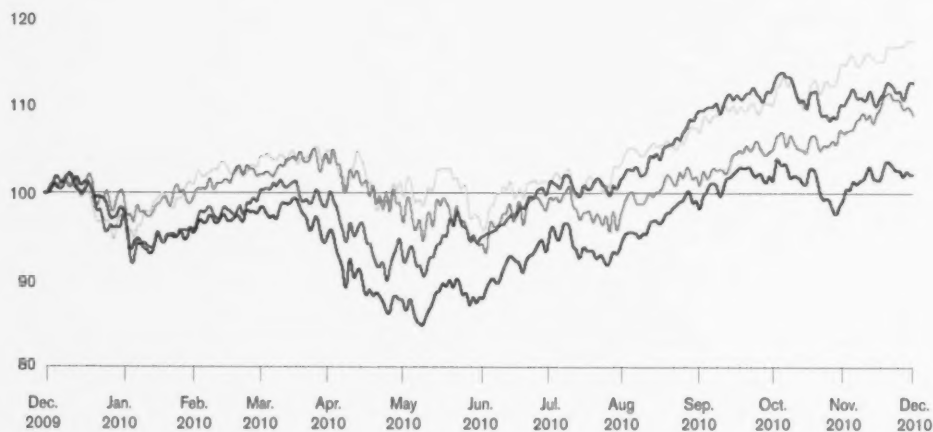
FIGURE 21

### EVOLUTION OF EQUITY MARKETS IN 2010<sup>1</sup>

(December 31, 2009 = 100  
– in local currency)

■ S&P TSX  
■ MSCI EM  
■ S&P 500  
■ MSCI EAFE

Source: Rimes



1. The description of the indexes is presented in Table 7, p. 28.

### Private Equity

The Private Equity portfolio posted a 26.7% return, outperforming its benchmark index by 2,474 b.p. (24.74%).

The portfolio showed resilience to the financial crisis and its after-shocks in 2008 and 2009, due to the quality of its assets. In 2010, the portfolio's high return was due to the combined effect of the good operational performance of the companies in the portfolio, increase in their EBITDA (earnings before interest, taxes, depreciation and amortization) and the notable reduction of their leverage, given this performance. The portfolio also benefited from the positive effect of rising stock markets on corporate valuations.

Leveraged buyout financing activities contributed nearly 50% to the portfolio's performance. At the same time, development capital activities account for nearly 25% of the return, largely due to the stake in Quebecor Media, given its portfolio weight and excellent performance.

In early 2010, as part of its new portfolio offering, the Caisse announced that the "Investments" component of the Investments and Infrastructures portfolio would be transferred to the Private Equity portfolio on July 1, 2010. For this reason, the Caisse adopted a new benchmark index that better represents the portfolio's activities and its new mandate. These changes were conveyed to the Caisse's depositors in April and implemented on July 1, as planned.

Table 22 shows how the new index affected the calculation of this portfolio's benchmark index.

Figure 23 shows that investments in the United States accounted for 48.9% of the portfolio's fair value as at December 31, 2010, followed by investments in Québec (19.8%) and Western Europe (19.6%).

FIGURE 23

### GEOGRAPHIC BREAKDOWN – PRIVATE EQUITY

(in percentage of fair value as at December 31, 2010)



TABLE 22

### COMPARISON OF THE RETURN OF THE INDEXES AND THE PRIVATE EQUITY PORTFOLIO

	Index	Return of the portfolio
	1 <sup>st</sup> half: old index 2 <sup>nd</sup> half: new index	1 <sup>st</sup> half: old mandate 2 <sup>nd</sup> half: mandate including Investments
1 <sup>st</sup> half	(7.4)%	14.6%
2 <sup>nd</sup> half	10.2%	10.5%
<b>Total 2010</b>	<b>2.0%</b>	<b>26.7%</b>

## Analysis of Performance by Asset Class

### OTHER INVESTMENTS

#### HIGHLIGHTS

**01** The Hedge Funds portfolio produced a 6.3% return, slightly outperforming its index.

**02** The new ABTN portfolio contributed \$509 million to net investment results. The provision related to these assets was reduced by \$1 billion.

**03** The Asset Allocation portfolio posted a negative return of \$77 million, reflecting the cost of defensive measures to protect the overall portfolio.

#### RETURNS ON THE PORTFOLIOS

##### Hedge Funds

The year 2010 was marked not only by a worldwide economic recovery, but also by market jitters and high volatility. The consolidation of the hedge fund industry continued in this environment, along with its evolution toward best practices in governance, transparency and alignment of interests with investors. This trend accelerated in the wake of the financial crisis, particularly under the leadership of the Hedge Fund Standards Board, bringing together hedge fund managers and major institutional investors, including the Caisse.

The Hedge Funds portfolio produced a 6.3% return, 11 b.p. (0.11%) above its benchmark index (see table 24). Directional strategies (i.e. Managed Futures) and strategies for distressed loans and emerging markets were the largest contributors to portfolio performance.

In 2010, the Caisse tightened its hedge fund selection criteria in favour of transparency.

##### ABTN

In a year that saw a sharp rise in public debt, corporations overall pursued their deleveraging efforts, contributing to narrower spreads. This improvement was particularly noteworthy in the United States.

In this environment, management of the new ABTN portfolio, created on January 1, 2010, translated into a \$509 million contribution to net investment results (see Table 24). This outcome is largely due to a \$781 million increase in the value of the portfolio's assets, buoyed by improving credit markets, reduced by the \$284 million cost of hedge transactions.

All in all, these results made it possible to reduce the ABTN provision from \$5.1 billion to \$4.1 billion. In addition, the borrowing associated with the portfolio was reduced by \$2 billion during the year. Finally, the portfolio's market risk was reduced by 54%.

### Asset Allocation and other activities

The goal of the consolidated asset allocation activities is to actively manage the asset allocation of the Caisse's overall portfolio over an investment horizon of less than three years.

There are two types of asset allocation activities:

- Activities carried out through the use of derivatives, particularly with the aim of protecting the portfolio against the risks of extreme fluctuation, and posted to the Asset Allocation portfolio.
- Activities tied to the overweighting and underweighting of specialized portfolios, the impact of which is applied directly to these portfolios.

In the wake of concerns over the economic outlook in Europe and the United States, and considering the Caisse's cash overexposure to certain riskier assets, such as Private Equity, Real Estate and ABTNs, defensive asset allocation measures were taken to protect the Caisse's overall portfolio against tail risks. The most important measures were overexposure to the U.S. dollar and underexposure to stock markets.

As at December 31, 2010, the Asset Allocation portfolio posted a negative return of \$77 million, particularly reflecting the cost of defensive measures taken to protect the Caisse's portfolio (see table 24). Overweighting and underweighting of specialized portfolios had a \$171 million negative impact on overall performance.

TABLE 24

### SPECIALIZED PORTFOLIO RETURNS – OTHER INVESTMENTS

(for periods ended December 31, 2010)

	Depositors' net assets \$B	1 year			5 years		
		Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)	Return %	Index <sup>1</sup> %	Spread <sup>2</sup> (b.p.)
<b>Hedge Funds</b>	<b>3.3</b>	<b>6.3</b>	<b>6.2</b>	<b>11</b>	2.1	1.4	79
<b>ABTN<sup>3,4</sup></b>	<b>(2.6)</b>	<b>\$509 M<sup>5</sup></b>	<b>N/A</b>	<b>N/A</b>	N/A	N/A	N/A
<b>Asset Allocation</b>	<b>0.6</b>	<b>\$(77)M<sup>5</sup></b>	<b>N/A</b>	<b>N/A</b>	<b>\$(1,792) M<sup>5</sup></b>	<b>N/A</b>	<b>N/A</b>

1. The description of the indexes is presented in Table 7, p. 28.

2. Compared to the benchmark indexes.

3. The ABTN portfolio financing exceeds the fair market value of its investments and mainly accounts for the negative net assets.

4. Since December 2007, the ABTN provision, combined with related costs and interest arrears, has totaled -\$5.2 billion. The effect on value added totaled 37 b.p. in 2010 and -82 b.p. over five years.

5. The net investment results in dollars are net of operating expenses and other fees. Results are combined for the five-year period.

# Changes in Assets

As at December 31, 2010, depositors' net assets amounted to \$151.7 billion, an increase of \$20.1 billion compared to \$131.6 billion a year earlier. Total assets under management stood at \$199.1 billion, down \$2.2 billion compared to 2009.

## HIGHLIGHTS

**01** Depositors' net assets increased by \$20.1 billion and stand at \$151.7 billion.

**02** Net investment results totalled \$17.7 billion.

**03** In 2010, the Caisse continued to strengthen its financial position, particularly by reducing its liabilities from \$39.1 billion to \$31.5 billion, a decrease of 19.5%.

## DEPOSITORS' NET ASSETS

In 2010, depositors' net assets increased by \$20.1 billion, with \$17.7 billion in net investment results and \$2.4 billion in depositors' net deposits.

Over the last five years, depositors' net assets climbed by \$29.5 billion, increasing from \$122.2 billion as at December 31, 2005 to \$151.7 billion as at December 31, 2010. This increase stems from, on the one hand, \$15.3 billion in net investment results and, on the other hand, \$14.2 billion in depositors' net contributions (see Table 25).

## DEPOSITORS' TOTAL ASSETS

As at December 31, 2010, depositors' total assets were \$183.2 billion, compared to \$170.7 billion as at December 31, 2009, an increase of \$12.5 billion (see Table 26). This rise stems mainly from the \$10.8 billion increase in investments. The Caisse also continued to strengthen its financial position, with a reduction of \$7.6 billion in liabilities, which fell from \$39.1 billion in 2009 to \$31.5 billion in 2010. Liabilities, primarily used to finance investment purchases, largely consist of short sales, securities sold under repurchase agreements, derivatives and financing programs issued by the Caisse's subsidiary, CDP Financial. The 2010 decrease in liabilities is largely due to the reduced use of securities sold under repurchase agreements.

TABLE 25

## ANALYSIS OF CHANGES IN DEPOSITORS' NET ASSETS

(for the period 2006-2010 – in billions of dollars)

	2006	2007	2008	2009	2010	2006-2010
<b>Net assets at beginning</b>	122.2	143.5	155.4	120.1	<b>131.6</b>	<b>122.2</b>
Income generated by the composition of the Caisse's benchmark portfolio (depositors' investment policies)	15.8	9.1	(29.3)	16.4	<b>13.0</b>	<b>24.9</b>
Added value	2.3	(0.9)	(10.2)	(4.4)	<b>5.1</b>	<b>(8.1)</b>
Operating expenses	(0.2)	(0.3)	(0.3)	(0.3)	<b>(0.3)</b>	<b>(1.3)</b>
Net investment results <sup>1</sup>	17.8	7.9	(39.8)	11.8	<b>17.7</b>	<b>15.3</b>
Depositors' net contributions	3.5	4.0	4.6	(0.3)	<b>2.4</b>	<b>14.2</b>
<b>Net assets at end</b>	<b>143.5</b>	<b>155.4</b>	<b>120.1</b>	<b>131.6</b>	<b>151.7</b>	<b>151.7</b>

1. Net investment results include cash activities.

## ASSETS UNDER MANAGEMENT AND ASSETS UNDER ADMINISTRATION

The \$14.7 billion decline in assets under management and assets under administration, presented at Table 26, stems from the sale of CW Financial Services (CW Capital) by its parent, Otéra Capital, representing \$11.0 billion in assets under administration as at December 31, 2009. It is also attributable especially to a \$1.7 billion drop in SITQ Group's assets under management and administration, due among others to the sale of Presima and a decrease in financing of \$1.8 billion by MCAP and Ivanhoe Cambridge. The latter is mainly attributed to the restructuring of the partnership with OMERS.

## NET INVESTMENT RESULTS

In 2010, the Caisse generated \$17.7 billion in net investment results, compared to results of \$11.8 billion the previous year (see Table 26).

Net investment results include investment income, reduced by operating expenses, external management fees, information technology repositioning charges, intangible asset write-offs, gains or losses on the sale of investments and unrealized gains or losses (see Table 26).

The analysis of operating expenses and external management fees is on page 128.

TABLE 26

## RESULTS AND EVOLUTION OF COMBINED NET ASSETS AND TOTAL ASSETS UNDER MANAGEMENT

(for years ended December 31 – in millions of dollars)

	2010	2009 <sup>1</sup>
Investment income	4,850	4,893
Less:		
Operating expenses	257	250
Expenses related to repositioning of the information technology and write-offs of intangible assets	34	–
<b>Net investment income</b>	<b>4,559</b>	<b>4,643</b>
Gains on the sale of investments	1,582	4,514
<b>Total realized income</b>	<b>6,141</b>	<b>9,157</b>
Unrealized increase in value of investments and liabilities related to investments	11,590	2,595
<b>Net investment results</b>	<b>17,731</b>	<b>11,752</b>
Depositors' net deposits (withdrawals)	2,423	(252)
<b>Increase in combined net assets</b>	<b>20,154</b>	<b>11,500</b>
Combined net assets, beginning of year	131,588	120,088
<b>Combined net assets, end of year</b>	<b>151,742</b>	<b>131,588</b>
Liabilities (primarily assets financed by borrowing)	31,455	39,068
<b>Depositors' total assets</b>	<b>183,197</b>	<b>170,656</b>
Assets under management	11,417	14,933
Assets under administration	4,516	15,676
<b>Assets under management and assets under administration</b>	<b>15,933</b>	<b>30,609</b>
<b>Total assets under management</b>	<b>199,130</b>	<b>201,265</b>

1. Certain figures from 2009 have been reclassified to conform to the presentation adopted in 2010.

## Changes in Assets

### Investment income

Investment income, also called current income, primarily includes interest income, dividends and real estate property rental income.

For the year ended December 31, 2010, investment income totalled \$4.9 billion, unchanged from a year earlier (see Table 26).

### Gains (losses) on the sale of investments

Gains on the sale of investments totalled \$1.6 billion in 2010, compared to \$4.5 billion in 2009. In 2010, \$4.1 billion in gains came from the sale of variable income securities, partly offset by \$2.4 billion in losses on the sale of fixed income securities.

### Unrealized gains (losses)

For 2010, the Caisse posted an \$11.6 billion unrealized gain on investments and liabilities related to investments, compared to \$2.6 billion in 2009 (see Table 27). Specifically, it saw \$5.0 billion in unrealized gains on shares and convertible securities, \$3.2 billion on bonds, \$1.7 billion on mortgages and \$1.1 billion on real estate.

In summary, net investment results in 2010 compare favourably to 2007, 2008 and 2009 (see Figure 28). As in 2009, each of its components – net investment income, gains (losses) on the sale of investments, unrealized gains (losses) – saw positive results (see Table 27).

FIGURE 28

### EVOLUTION OF NET INVESTMENT RESULTS

(for years ended December 31 – in billions of dollars)

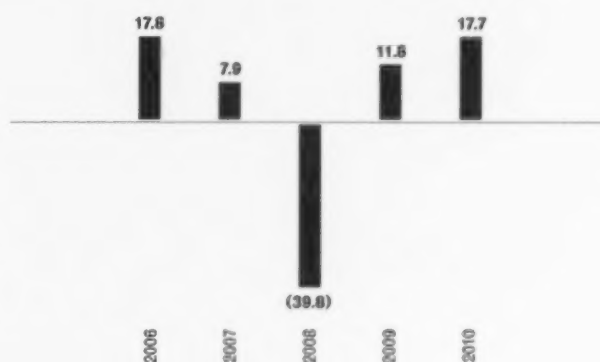


TABLE 27

### BREAKDOWN OF NET INVESTMENT RESULTS

(for periods ended December 31 – in billions of dollars)

	2006	2007	2008	2009	2010	2006-2010
Net investment income	5.3	6.2	5.8	4.7	4.5	26.5
Gains (losses) on the sale of investments	4.6	9.4	(23.2)	4.5	1.6	(3.1)
Unrealized increase (decrease) in value of investments and liabilities related to investments	7.9	(7.7)	(22.4)	2.6	11.6	(8.1)
Net investment results	17.8	7.9	(39.8)	11.8	17.7	15.3

## DEPOSITORS' NET DEPOSITS (WITHDRAWALS)

As at December 31, 2010, total depositors' net deposits stood at \$2.4 billion, compared to net withdrawals of \$0.3 billion in 2009. This difference is mainly due to the large deposits of one depositor, Fonds d'amortissement des régimes de retraite (FARR), which did not make any deposits in 2009.

## NEW OPERATIONAL AND INFORMATION TECHNOLOGY BUSINESS MODEL

In 2010, the Caisse continued to implement a new customer-focused business model started in 2009.

This new business model, which aims to optimize the level of overall IT-Operations service delivery, relies on the complementary expertise and collaboration of the Operations and Information Technology teams. It can effectively support the Caisse by encouraging greater proximity with the managers of the various investment groups and enabling IT-Operations teams to be more agile, flexible and fast. It will provide greater control in terms of operations and continuity of the Caisse's IT services.

The activities, in particular, endowed the institution with strategic IT organization functions and boosted the number of key permanent personnel. The introduction of the new model was also an opportunity to review the role of certain providers and start simplifying the Caisse's application portfolio.

An important element of the new business model is also to adopt enterprise architecture to continue simplifying the way we work and reducing the complexity of, for instance, our application interrelationships.

To ensure alignment with the Caisse's business priorities, we established a new IT and Operations governance structure, involving all Caisse units. It is led by a strategic committee whose members are appointed by the Executive Committee.

The repositioning of Information Technology, restructuring of the IT and Operations teams and termination of certain IT projects in development resulted in a total non-recurring charge of \$34 million.

Ultimately, these measures will generate annual recurring Operations and IT group savings of about \$25 million.

# Risk Management

## HIGHLIGHTS

**01** Integration of the risk-return concept into day-to-day investment operations.

**02** Reduction of the overall portfolio's absolute and active risk, providing the Caisse with additional leeway.

**03** Strengthening of risk management tools and practices to better identify and quantify risks.

**04** Development of a risk culture based on collaboration between the investment and Risk teams.

## RISK MANAGEMENT AT THE CAISSE IN 2010

In 2010, risk management continued to be a fundamental strategic priority of the Caisse. The Caisse's primary objective is to develop advanced tools and rigorous mechanisms to continue increasing its ability to identify, quantify and oversee risks. This, in turn, increases the institution's abilities and agility to perform and produce the expected returns in an environment marked by turbulence and volatility.

As a result, many steps were taken to develop the leeway the Caisse must have to take advantage of market opportunities while maintaining an optimum risk-return balance. Throughout the year, the Caisse launched several initiatives to continue strengthening its risk management practices and tools. Many of these initiatives contributed to the development of a risk culture based on active collaboration between the investment and Risk teams. The Caisse also consolidated its governance model in this area.

Through these efforts, the Caisse pursued its goal of being an agile investor, capable of meeting the challenges related to its expertise. It can now rely on a key tool: more robust and strategic risk management.

## INITIATIVES TO MANAGE ITS FINANCIAL RISKS

In 2010, the Caisse carried out several strategic initiatives to reduce its market, liquidity, credit and counterparty risks. This allowed the institution to develop greater leeway to manage investments and conduct investment activities.

### ABTN

During the first half of the year, the Caisse made certain hedging transactions that substantially reduced this portfolio's attributable risk. This had the effect of protecting the ABTN portfolio against downturns in the market for this type of product and potential underlying credit losses.

### Leverage reduction

The Caisse eliminated the leverage in its Private Equity and Infrastructure portfolios and continued its leverage reduction strategy in the Real Estate portfolio. It eliminated \$700 million in Private Equity portfolio leverage and reduced the leverage inherent in this portfolio's major investments. The leverage of its Real Estate portfolio (total debt versus total assets) fell from 56 % as at December 31, 2009 to 47% as at December 31, 2010, representing a \$3.7 billion decrease.

For the Caisse, the leverage ratio (liabilities versus total assets) continued to decline, reaching 17% as at December 31, 2010, compared to 23% as at December 31, 2009 and 36% as at December 31, 2008.

### Matching sources and uses of funds

The Caisse continued its \$8 billion financing program announced in the fall of 2009. This was completed in June 2010. The financing served to repay short-term debt and better match financing sources with financed real estate assets. This financing did not increase the Caisse's leverage and helped reduce the liquidity risk.

### European crisis

The Caisse proactively implemented an underweighting strategy in portfolios specifically exposed to the consequences of the European crisis. Due to an improved economic outlook, it reduced this hedge in the second half of the year.

### Rising interest rates

In the fall of 2010, the Caisse adopted a hedge strategy against contingent interest rate increases, when these rates had fallen to very low levels.

### Real estate debt

The portfolio's exposure to foreign markets (higher risk) declined from 33.0% to 17.8%, representing a decrease of \$1.6 billion. In addition, the portfolio's subordinated debt portion (high risk) was reduced by \$732 million, falling from 13.5% to 6.4%.

### Bonds

The implementation of the Caisse's new portfolio offering to the depositors and the review of investments eligibility in the Bonds portfolio investment policy led to a lower weight in commercial mortgage backed securities.

## IMPACT ON RISK MEASUREMENTS

The deployment of these different initiatives had a tangible impact on the Caisse's risk level, confirmed by our risk measurements.

### Absolute and active market risk

As a result, absolute and active risk levels declined substantially in 2010. Relative to its benchmark portfolio, the Caisse portfolio's excess absolute risk was reduced substantially (see Figure 29). This reduction in the overall risk level mainly occurred between March and September 2010 – when the ABTN hedge transactions and the Equity class weighting adjustments were made.

Tables 30 and 31 and Figures 32, 33 and 34 show the changes in the absolute and active risks of the Caisse portfolio and its main components.

TABLE 30

### MARKET RISK – ABSOLUTE

(as a percentage of total net value of the class as at December 31)

Classes	2010	2009
Fixed Income	10.3	9.3
Inflation-Sensitive Investments <sup>1</sup>	35.5	49.6
Equity	51.4	51.5
Other Investments <sup>2</sup>	2.2	6.0
<b>Total</b>	<b>34.3</b>	<b>38.1</b>

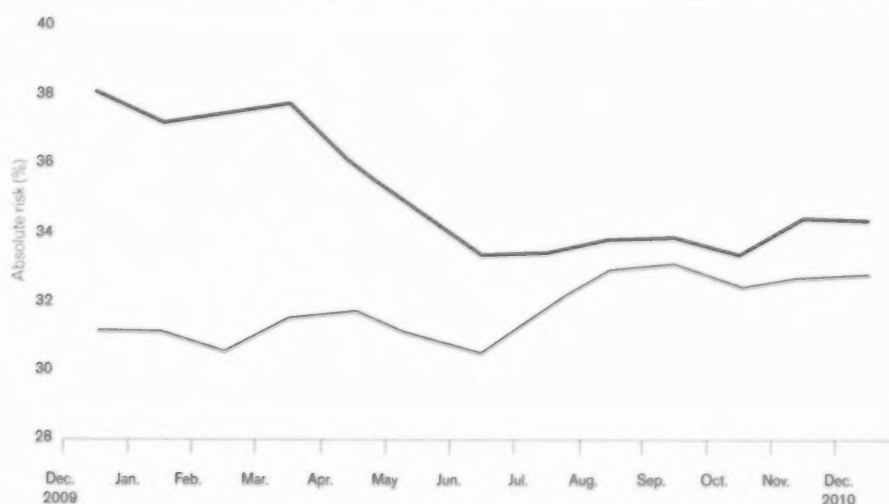
1. The Investments and Infrastructures portfolio was included in this subdivision for 2009.

2. The risk of the Other Investments class is presented as a percentage of the Caisse's net assets. This class contains the Hedge Funds, ABTN and Asset Allocation portfolios.

FIGURE 29

### MARKET RISK – ABSOLUTE

■ Caisse portfolio  
■ Benchmark portfolio



## Risk Management

TABLE 31

**MARKET RISK – ACTIVE**

(as a percentage of total net value of the class as at December 31)

Classes	2010	2009
Fixed Income	1.3	2.8
Inflation-Sensitive Investments <sup>1</sup>	11.0	20.9
Equity	6.2	7.3
Other Investments <sup>2</sup>	2.1	5.8
<b>Total</b>	<b>4.5</b>	<b>10.3</b>

1. The Investments and Infrastructures portfolio was included in this subdivision for 2009.
2. The risk of the Other Investments class is presented as a percentage of the Caisse's net assets. This class contains the Hedge Funds, ABTN and Asset Allocation portfolios.

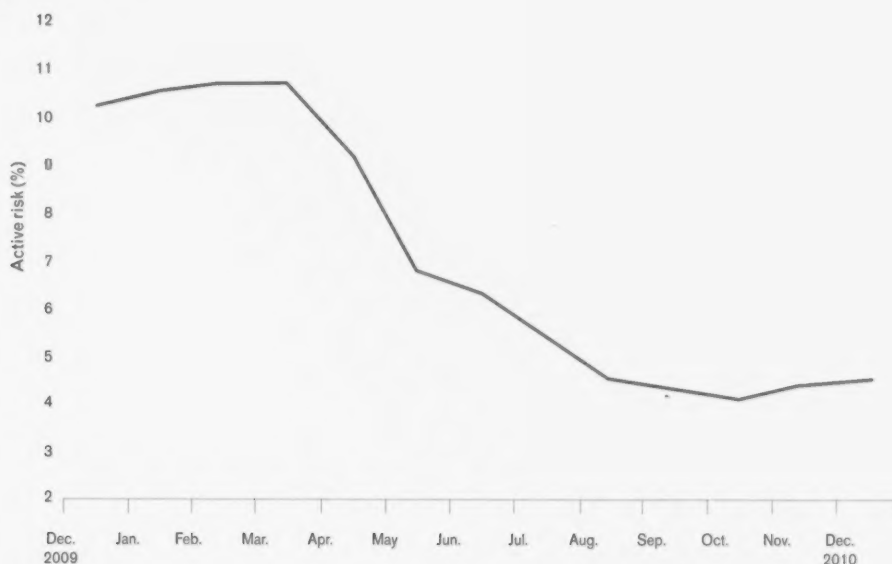
Figure 33 shows that the reduction of absolute risk in the Caisse portfolio is mainly due to hedging transactions in the ABTN portfolios (Other Investments class), reducing its risk by 54%, and leverage reduction in the Real Estate portfolio (Inflation-Sensitive Investments class). The increase in absolute risk as a percentage of the Caisse's total assets in the Equity component is due to the increase in the net value of the investments in this class. The reduction of the absolute risk in the ABTN and Real Estate portfolios provided the Caisse with leeway to increase its equity investments during the year.

As Figure 34 shows, there was a concerted reduction in active risk. The 56% decline in active risk is not due to a single decision or transaction but a series of initiatives, particularly ABTN hedging transactions, reduced Real Estate portfolio leverage and the adoption of more representative benchmark indexes for the illiquid portfolios.

FIGURE 32

**MARKET RISK – ACTIVE**

■ Caisse portfolio



**Liquidity risk**

Favourable market developments and leverage reduction contributed to the increase in available liquidity.

The marked reduction in the volume of over-the-counter derivatives following the simplification of the portfolio offering reduced the Caisse's exposure to fluctuations in the fair value of these instruments. This decrease led to a reduction in potential collateral calls and, in turn, lower liquidity risk. As at December 31, 2010, our liquidity risk management tools reveal that the Caisse's liquidity remains at a reasonable level.

**Credit risk**

The exposure of the Caisse portfolio to a deteriorating credit market was reduced in 2010, due to ABTN hedging transactions, changes in the Real Estate Debt portfolio composition and certain provisions arising from the integration of company credit operations into the Bonds portfolio. Our credit risk measurements indicate that the general improvement of credit market conditions helped reduce Caisse portfolio risk.

FIGURE 33

**MARKET RISK – ABSOLUTE**

(as a percentage of Caisse's net assets)

■ December 31, 2009  
■ December 31, 2010

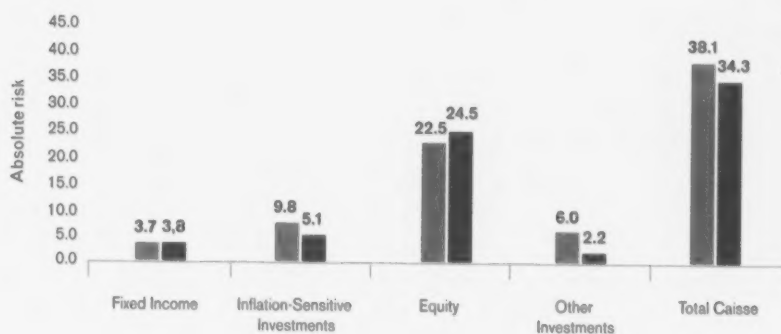
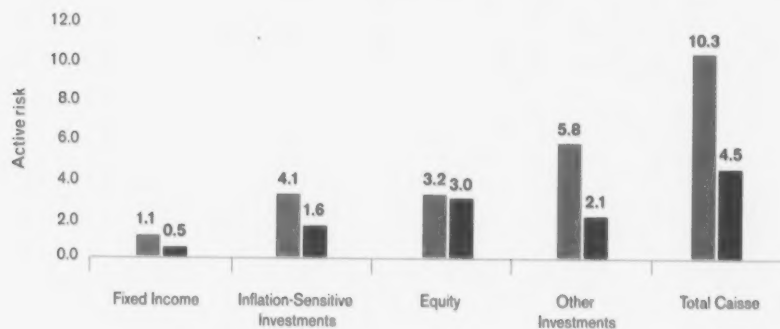


FIGURE 34

**MARKET RISK – ACTIVE**

(as a percentage of Caisse's net assets)

■ December 31, 2009  
■ December 31, 2010



## Risk Management

### Counterparty risk

In 2010, the Caisse continued to reduce the use of over-the-counter derivatives, which effectively reduced counterparty risk. The volume of over-the-counter derivatives fell by over 50% during the year and exposure (without netting) decreased by about \$1.5 billion. The ISDA<sup>1</sup> agreements negotiated by the Caisse kept exposure to its counterparties at low levels. In addition, the implementation of a process of forward-looking counterparty credit risk analysis improved the understanding and active management of this risk.

Figure 35 shows that counterparty risk exposure declined during the year.

### IMPROVEMENT OF RISK MANAGEMENT METHODOLOGIES AND TOOLS

In 2010, the Caisse took several steps to continue improving its methodologies and tools as well as strengthening its oversight and processes in risk management.

#### Deployment of credit VaR

Analysis, monitoring and calculation of the credit VaR of the Fixed Income portfolios and the Québec International portfolio were implemented in 2010. The Caisse now has a high-performance tool that better manages this type of risk, by analyzing the changes in the quality of the positions in these portfolios.

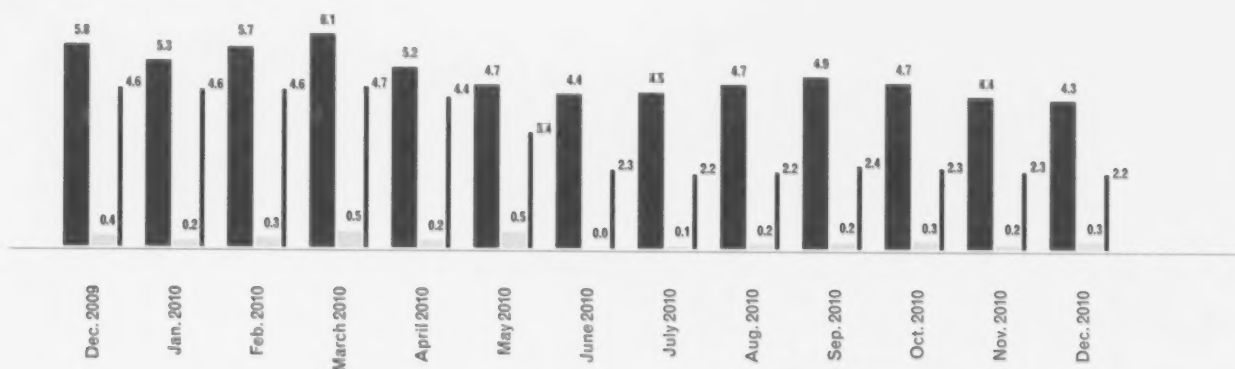
1. Agreements made in accordance with the basic document proposed by the International Swap Dealer Association.

FIGURE 35

### EVOLUTION OF THE EXPOSURE TO COUNTERPARTY RISK<sup>1</sup>

(in billions of dollars)

- Exposure without payments being offset
- Exposure according to negotiated ISDA agreements
- | Number of over-the-counter contracts (in thousands)



1. This figure excludes the counterparty risk incurred directly by the real estate subsidiaries and the hedges related to ABTNs.

### **Deployment of a counterparty credit risk monitoring process**

Close collaboration between the Risk and investment teams led to the implementation of a forward-looking counterparty credit risk analysis process. Monitoring was also set up to assess the default risk of each Caisse counterparty. This monitoring is based on quantitative indicators and the fundamental analysis performed by various investment teams. The process will allow the Caisse to identify high-risk counterparties and act, whenever necessary, to reduce inherent risks.

### **Integration of information from the real estate subsidiaries into the liquidity and counterparty risk analysis**

During 2010, the information from the real estate subsidiaries was consolidated and integrated into the counterparty risk exposure and liquidity risk calculations, increasing the precision of the analysis.

### **Addition of new stress tests**

In addition to the scenarios that were integrated into monthly monitoring, the Caisse implemented several additional tail risk scenarios to manage the risk of such situations. The new tests were added for three categories of shocks:

- Single factor shocks: sharp movements in Canadian real estate.
- Historical shocks: 1994 bond crisis and Russian default of 1998.
- Hypothetical shocks: major decline of U.S. consumption, default of Greece and the sharp increase in inflation in China.

### **Implementation of new back-testing practices**

In 2010, the Caisse considerably strengthened its back-testing practices to ensure the quality of its risk measurements, particularly for market VaR.

### **Improvement of methods for calculating liquidity risk**

The methodology for assessing liquidity risk is based on potential excess liquidity scenarios. This potential excess liquidity is due to the difference between the forecasts and the needs of potential sources according to various financial crisis scenarios. In 2010, calculation of the potential needs for margin and collateral was improved by integrating information about equity lending and borrowing instruments and by specifying the market risk of derivatives.

### **Strengthening and development of market risk breakdown functionalities**

In 2010, new functionalities were developed to integrate the characteristics specific to the portfolios and the risk factors. The investment teams now have access to more granular information on the source of their portfolio's risk.

### **Integration of interest rate and foreign exchange volatility products**

This method, implemented in 2010, makes it possible to account for the impact of a variation in the volatility of interest rate and foreign exchange options, improving the practicality of market risk measurements.

### **Optimization of operational efficiency**

In 2010, we reviewed, automated and began to centralize the data upstream from the market VaR production processes, increasing the value of the data and the efficiency of risk measurement production.

## **REVIEW OF OVERSIGHT AND PROCESSES**

### **Investment policy review**

In 2010, the Caisse continued its investment policy review by reviewing the policies of 12 specialized portfolios, including Canadian Equity, Global Equity, Bonds, Québec International, Short Term Investments, ABTN, Real Estate Debt, Real Estate, Infrastructure, Private Equity, Hedge Funds and Asset Allocation. Each of these investment policies was adopted by the Board of Directors and establishes the philosophy, management style, investment universe, benchmark index, value added objective and risk oversight.

The investment policy review aimed to achieve the following:

- Review the universe of eligible investments.
- Review of the concentration and risk limits.
- Ensure better risk oversight.
- Increase the transparency of the investments.

The collaboration and disciplined approach of our investment, research, depositor relations and risk teams allowed us to accomplish the above.

## Risk Management

### Revision of the Integrated Risk Management Policy (IRMP)

In 2010, a new chapter on risk limit management was added to the IRMP. The objective is to prevent managers from exceeding the limits of the investment policies and the IRMP – in addition to clearly defining the roles and responsibilities of each stakeholder.

These efforts led to the establishment of the “yellow indicator” concept, ensuring proactive risk management. When the yellow level is reached, even if the limits are still respected, discussions are initiated immediately between the Risk team, Compliance and managers concerned to manage the situation.

A credit risk chapter was approved in 2010 and incorporated into the IRMP. This chapter describes the main guidelines for credit risk management at the Caisse.

### Overall Caisse concentrations

In 2010, the Caisse improved the monitoring of its overall concentration levels. A new report was implemented and presents a detailed image of the geographic and sector concentration by specialized portfolio and for all Caisse investments.

### Oversight of equity lending and borrowing operations

To ensure effective management of the business, financial and operational risks related to the equity lending and borrowing operations performed by the Caisse and its custodians, the Caisse adopted oversight for this type of activity. This is based on the industry's best practices and favours a risk-return balance. The oversight management framework specifies the governance, responsibility sharing and counterparty selection process. It also sets certain limits for overseeing this activity.

### Redesign of the management mandate guide

The application of the management mandate guide (MMG), which is derived from the investment policies and used by the different teams, was entirely redesigned in order to improve functions pertaining to approval, research, integration of information and data management.

### Implementation of the operational incident and loss collection process

The operational incident and loss collection process was formalized at the beginning of 2010. This process allows proactive management of operational incidents by analyzing the causes of these events. The implementation of corrective actions, if required, strengthens the management process and reduces the probability that a similar incident will occur.

### Review of the operational risk indicators

A review of the Caisse's operational risk indicators was undertaken in 2010. These indicators allow the Caisse to monitor the changes in risk level (such as staff turnover rates and delays in OTC derivative trade confirmations) or monitor the risk control measures (such as business continuity plans). The Caisse's practices were calibrated and new indicators were proposed to the main business units. Their implementation is scheduled for 2011.

## INTEGRATION OF RISK-RETURN DIALOGUE

Risk management is inseparable from the investment and portfolio management processes. Since the investment teams must intentionally take risks to generate expected returns, the risk-return relationship is an integral part of investment activities. In this sense, robust risk management is indispensable for ensuring that our managers take and control calculated risks.

In 2009, the Caisse saw major changes in risk management governance and, to a greater extent, the establishment of greater transparency of the Caisse's investment activities. The clarification of the investments covered by the investment policies, segmentation of the assets held in each portfolio, establishment of a risk measurement for each portfolio relative to returns, and analysis of the different concentrations and risk factors, are part of the report for each of the Caisse's risk management committees.

The risk-return reports, which are the core of our approach, provide an in-depth analysis of every activity, results obtained and risk assessments. In 2010, the Risk and investment teams collaborated to continue the implementation of risk-return reports, improving their quality, simplifying them and facilitating their understanding by the Board of Directors' Risk Management Committee. The reports have also evolved in tandem with the investment policies. They have served to reinforce the risk-return dialogue within the Caisse.

For example, during the European sovereign debt crisis at the beginning of 2010, a working group, consisting of investment teams, economists and the Risk team, was formed by the Caisse. The working group began by defining the stress tests, which were performed by the Risk team. Upon identifying the Caisse global portfolio's vulnerabilities, the working group developed strategies to guard against a worsening of the crisis, including an underweighting strategy in the portfolio of publicly-traded securities. The working group subsequently monitored the day-to-day implementation of these strategies.

Similarly, the Risk and investment teams also worked together to support compliance with risk oversight. Action plans were developed to ensure the implementation of the required adjustments. These action plans were monitored in collaboration with the investment teams.

As a result, throughout the year, a dialogue was established between the investment and Risk teams. The involvement of the Risk team with the portfolio managers along with the constructive criticism this team brings to the table have become entrenched in the Caisse's approach, strengthening the institution's risk culture.

The risk management team is continuing to develop its approach to go "beyond measurement" in order to ensure healthy oversight of risks and added value with managers.

## THE RISK GOVERNANCE MODEL

To ensure a risk-return balance in the performance of its second-level of risk control, the Risk team's strategy is based on the following:

- Integration of risk experts working in concert with each of our investment teams.
- Development of high-performance analytical tools.
- Integration of the risk component into the Caisse's business processes.
- Development of a better understanding of the risks arising from the Caisse's operations.

This strategy is consistent with the overall risk management approach adopted by the Caisse and described in its Integrated Risk Management Policy.

## Integrated Risk Management Policy

The Caisse adopted a global and centralized approach for risk management oversight: the Integrated Risk Management Policy (IRMP).

This policy is reviewed regularly and is aimed at fostering a disciplined risk management culture and practices. More specifically, the IRMP defines risk management governance at the Caisse, sets the level of acceptable risk to prevent excessive losses, aligns this level of risk with value-added objectives and aims to allocate risk effectively.

The IRMP is the cornerstone of risk oversight. It includes reporting mechanisms and describes different aspects of risk management, particularly:

- The guiding principles, namely the risk model and the independence of the support teams in integrated risk management.
- The organizational structure, the normative framework, governance and sharing of responsibilities.
- Risk budgets.
- Limits on transaction authorization, management outsourcing and concentration by issuer.
- A framework for management outsourcing and the use of financial derivatives.
- The management of various risks.

## Levels of control

Risk management is ultimately the responsibility of the Board of Directors. However, managers at all levels are required to integrate risk management into their decisions every day. It applies to all Caisse employees and agents in the fulfillment of their duties.

Governance of risk management is based on three levels of control:

**Level 1** – The portfolio managers, who are primarily responsible for managing risks related to operations under their purview.

**Level 2** – The Risks Committee (RC), a subcommittee of the Executive Committee, with assistance from the Risk group and the Senior Vice-President, Policies and Compliance.

**Level 3** – The Board of Directors and its Risk Management and Audit Committees – in addition to the Internal Audit division.

In order to ensure necessary objectivity and rigour, teams independent of those in investments, are responsible for defining and overseeing the IRMP and the investment policies of the specialized portfolios, as well as monitoring their application.

## Risk Management

### Investment policies and risk budgets

The purpose of investment policies is to provide oversight for portfolio manager work. Each specialized portfolio has an investment policy that defines the investment philosophy, management style, investment universe, benchmark index, value-added objective and risk oversight, including concentration and risk limits.

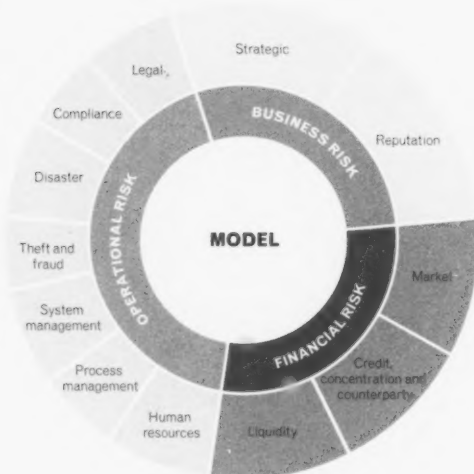
A risk limit, or risk budget, is set for each specialized portfolio and the Caisse's overall portfolio. This risk budget takes into account the value-added objectives for each portfolio. For the Caisse's overall portfolio, the risk limit reflects the diversification effect of the specialized portfolios.

### RISK MODEL

At the Caisse, the risk model is the basis for identifying, assessing and managing risks. It establishes a common language to ensure the various stakeholders can communicate effectively about risk management. The risk model is also a basis for the rigorous and exhaustive analysis of each risk. Ultimately, this process leads to the implementation of investment strategies that generate stable and sustained returns to meet the depositors' expectations.

FIGURE 36

### THE CAISSE'S RISK MODEL



Within this model, the risks inherent in the Caisse's activities are divided into three broad categories: business, financial and operational risks (see Figure 36). Each category consists of sub-categories for accurately identifying all possible risks. Each risk requires a specific management approach.

### Business risks

#### Strategic risk

Strategic risk is the possibility that an event related to the practices or relationships of the Caisse, its subsidiaries or employees will contravene its mission, culture and fundamental values.

Strategic risk is also related to the inadequacy of business strategies or deficiencies in the implementation of the Caisse's strategic orientations. Lastly, the Caisse will be exposed to strategic risk if its resources are not allocated according to the set priorities.

The Caisse manages this risk using a structured strategic planning process that involves all of its units. Strategic orientations are proposed by the Executive Committee, approved by the Board of Directors and communicated to all employees. Annual business plans are subsequently drawn up. The members of the Board of Directors and the Executive Committee receive regularly a summary of the Caisse's activities.

#### Reputation risk

Reputation risk is the possibility that an event related to the business practices or relationships of the Caisse, its subsidiaries or its employees will adversely affect the Caisse's image or cause the public to lose confidence in the institution. This risk could detract from the Caisse's ability to achieve its objectives.

All directors, members of senior management and employees are responsible for carrying out their activities to minimize reputation risk.

The Caisse manages and controls this risk through codes of ethics and professional conduct for officers, directors and employees, training programs, effective internal management and governance practices and various policies and procedures, including its Policy on Responsible Investment. The Caisse also ensures that the information it provides internally and externally is truthful and corroborated. It aims to ensure that the public and the media gain a better understanding of its operations. The Caisse also monitors relevant communications reports and responds by taking public positions, whenever necessary.

**Financial risks****Market risk**

Market risk represents the risk of financial loss arising from changes in the value of financial instruments. The value of a financial instrument may be affected by changes in certain market variables, such as interest rates, foreign exchange rates, share prices and commodity prices. The risk arises from the volatility in prices of financial instruments, which, in turn, result from the volatility of such market variables.

The Caisse manages all market risks in an integrated manner. The main elements that give rise to risks such as industry, country and issuer are taken into account. To manage market risk, the Caisse may use derivative financial instruments that are traded on exchanges or directly with banks and securities dealers.

**Value at risk**

The Caisse measures market risk using a statistical technique known as value at risk (VaR). This technique, used by most investment firms and financial institutions, covers all the assets held by the Caisse. The Caisse determines the VaR for each instrument in its specialized portfolios and aggregates the information for the overall portfolio. Two types of risk are assessed, namely the absolute VaR of the Caisse's benchmark portfolio and overall portfolio, and the VaR of active management.

VaR is based on the statistical measurement of volatility of the market value of each portfolio position and their correlations. VaR uses historical data to estimate the loss expected during a given period according to a predetermined confidence level. For example, using a 99% confidence level, the VaR indicates that a loss will exceed this level in only 1% in cases for a given period.

One of the advantages of VaR is that it includes the risk of a wide range of investments in a single measurement, providing an overall risk measurement for a portfolio and even for a set of portfolios.

The Caisse uses the historical simulation approach to assess VaR. The historical simulation method is based primarily on the assumption that the future will be similar to the past. This method requires a series of historical data for all the risk factors necessary to assess the returns on instruments. In the absence of such historical data, particularly for less liquid products, such as private equity and real estate, substitute securities and various mathematical models are used to calculate VaR. Historical data from 1,300 days of observation of risk factors such as variations in exchange rates, interest rates and financial asset prices, is used to assess the volatility of returns and the correlation between returns of various assets.

The results of the calculations obtained by applying this methodology do not allow an estimate, based on a specific event, of the amount of the loss that a portfolio would incur if such an event occurred.

This methodology used by the Caisse is intended to estimate a portfolio's risk by annualizing its potential daily loss (i.e. by assuming that the lost amounts throughout the year will be reinvested to maintain the same level of risk). In short, this methodology means that the effects of the worst adverse events on the portfolio over a one-day horizon will be repeated several times a year.

It is inappropriate to make a connection between the calculation of VaR at 99% used by the Caisse and a specific historical event. This methodology is not designed for this objective. It seeks to provide the Caisse's managers with the means to assess and manage portfolio risk dynamically.

VaR measures risk under normal market conditions. Therefore, losses realized may greatly differ from the VaR when the historically observed interrelationship between risk factors is disrupted.

As VaR is not designed to be used on its own, the Caisse uses complementary limits and measurements. For example, the investment policies are used to define concentration limits (geographic, sector, instrument type, issuer, etc.) as well as loss limits.

## Risk Management

### ***Absolute risk and active risk***

Any investment decision involves an element of risk, including the risk of a gain or loss arising from a fluctuation in the value of financial instruments held in a portfolio. The same method is used to calculate the absolute risk of the Caisse's benchmark portfolio and overall portfolio.

The absolute risk of the benchmark portfolio is the result of the risk of the benchmark indexes related to the asset classes that make up the portfolio at a given date. For example, if the depositors decide to increase the bond weighting and reduce the weighting of publicly-traded equities in their respective benchmark portfolios, the risk will automatically decrease, given the lower volatility of bonds. By the same token, the expected long-term absolute return will also decrease.

The absolute risk of the overall portfolio is the result of the risk of the positions that make up the Caisse's overall portfolio at a given date.

Active risk represents the possibility that the Caisse's return will diverge from the benchmark portfolio return due to active management of its portfolio. The greater the active risk, the more the overall portfolio's expected absolute return (see Figure 37) will diverge from the benchmark portfolio return.

The absolute risk of the Caisse's benchmark portfolio and the active risk and the absolute risk of the overall portfolio are measured regularly and are subject to various limits.

### ***Stress tests***

The Caisse also uses stress tests to assess the losses of a specialized portfolio and the overall portfolio in extreme circumstances. The stress test is a risk measurement that complements VaR by estimating the impact of extreme circumstances on returns. These circumstances have a low probability of occurring but are likely to give rise to substantial losses. Using different types of extreme scenarios, the stress test measures the loss of value of a position following a variation in one or more usually interrelated risk factors such as equity prices, interest rates, credit spreads, foreign exchange rates, commodity prices and market volatility.

Like VaR, the stress test includes the risk of many positions in a single overall measurement, making it possible to analyze losses for a portfolio or for a set of portfolios, under selected extreme scenarios.

### **Credit, concentration and counterparty risk**

#### ***Credit risk***

Credit risk is the possibility of a loss of market value in the event a borrower, an endorser, a guarantor or counterparty does not honour its obligation to repay a loan or to fulfill any other financial obligation, or experiences a deterioration of its financial situation.

Credit risk analysis includes calculating the probability of default and the recovery rate on debt securities held by the Caisse, as well as monitoring changes in credit quality of issuers and groups of issuers<sup>1</sup> whose securities are held in any of the Caisse's portfolios. In managing credit risk, the Caisse frequently monitors changes in the ratings issued by agencies and compares them with in-house credit ratings, whenever available. It also uses the credit VaR for its specialized Bonds, Long Term Bonds and Real Return Bonds portfolios.

The credit VaR is a statistical measurement that integrates the information on the current and potential creditworthiness of issuers in the portfolio, their interrelations and the level of loss in case of default. This measurement therefore allows assessment of the forecast loss over a period according to a specified confidence level. The Caisse assesses the credit VaR over a one-year period for a 99% confidence level.

#### ***Concentration risk***

Concentration risk analysis measures the fair value of all the financial products related to a single issuer or a group of issuers<sup>1</sup> with similar characteristics (geographical area, industry, credit rating).

The concentration limit by group of issuers is set at 3% of the Caisse's total assets. Securities issued by the Government of Canada, the Québec government or any other Canadian province or territory or by their ministries or departments and agencies are exempt from this calculation as they are not subject to concentration limits. Sovereign issuers with AAA credit ratings are also excluded from this concentration limit. Lastly, specific concentration limits apply to investments in emerging markets.

1. A group of issuers is controlled by a parent company.

**Counterparty risk**

Counterparty risk is the credit risk from current or potential exposure to over-the-counter derivatives resulting from the Caisse's operations.

Transactions involving derivatives are carried out with financial institutions whose credit rating is established by recognized rating agencies and for which operational limits are set by senior management. Moreover, the Caisse enters into legal agreements based on the standards of the International Swaps and Derivatives Association (ISDA)<sup>1</sup> to benefit from the netting of amounts at risk and the exchange of collateral. In this way, the Caisse limits its net exposure to this credit risk.

Current exposure to counterparty risk is measured daily, under the legal agreement in effect. Potential exposure to counterparty risk is measured monthly.

**Liquidity risk**

Liquidity risk is the possibility that the Caisse may not always be able to fulfill its commitments regarding its financial liabilities without having to obtain funds at abnormally high cost or proceeding with a forced sale of assets. It also corresponds to the risk that it may not be possible to sell investments rapidly or to invest without having a significant adverse impact on the price of the investment in question.

Compliance with preset rules is reviewed every month, in addition to the daily monitoring of liquidity. The Caisse simulates various scenarios to estimate the potential impact of different market events on its liquidity situation. The managers responsible assess the liquidity of the markets on which the Caisse's financing operations are based. They also ensure the Caisse is active in various financial markets and maintains relationships with credit rating agencies that rate the Caisse as well as providers of capital.

1. The ISDA promotes sound risk management practices and issues legal opinions on netting and collateral arrangements.

FIGURE 37

**COMPONENTS OF THE CAISSE'S RISK AND RETURN**

## Risk Management

### **Operational risks**

Operational risk corresponds to the possibility of direct or indirect financial loss resulting from the deficiencies within the operations.

Operational risk management and assessment require the self-assessment of risks, listings of incidents, the use of indicators and maintenance of rigorous processes.

### **Human resources management risk**

The risk related to human resources management includes such elements as recruiting and retention (recruiting competent, honest and motivated personnel), training (maintaining and developing employee competencies) and evaluating performance and compensation (ensuring fair, equitable and competitive compensation based on performance).

### **Process management risk**

The risk arising from process management is related to the processes for input, settlement and tracking of transactions, and errors that may arise in the execution of the processes in place. In addition to internal causes, this risk may arise from the poor quality of services rendered by subcontractors, suppliers and business partners.

### **System management risk**

The Caisse is exposed to a risk in the event of deficiency of its information technology infrastructures or computer systems. This deficiency may result from a breakdown or other malfunction that may cause delays or an interruption in operations that is not caused by a disaster.

### **Theft and fraud risk**

This is the risk of losses arising from intentional acts to defraud, to embezzle funds or to appropriate the assets of the Caisse or its depositors.

### **Disaster risk**

The disaster risk represents the risk of losses resulting from the interruption of business following a natural or other disaster.

### **Compliance risk**

Compliance risk corresponds to the risk of losses as a result of non-compliance with regulatory obligations, with policies and directives, or with professional and ethical standards and practices specific to the Caisse's operations. It occurs in the event that the Caisse fails to fulfill its duties.

### **Legal risk**

Legal risk is related to the rights and obligations associated with the Caisse's operations and the legislative framework under which they are carried out. Important aspects of legal risk are related to compliance with laws and regulations to which the Caisse and its management teams are subject. They also depend on the assurance that the agreements entered into by the Caisse accurately reflect the planned transactions and contain the appropriate provisions. Legal risk also refers to the risk of lawsuits that may affect the Caisse.

# Compliance

## HIGHLIGHTS

**01** Implemented a rigorous monitoring system to prevent any breach of the limits established in the investment policies of the specialized portfolios.

**02** Provided depositors with semi-annual certification of compliance with the investment policies of the specialized portfolios and their investment policy.

**03** Processed more than 50 information access requests.

The Caisse complies with its incorporating act and various laws that apply to its activities. It particularly ensures compliance with depositors' investment policies, specialized portfolio investment policies and its language policy.

## INVESTMENT POLICIES

In 2010, certificates of compliance with depositors' and specialized portfolios' investment policies were sent to depositors twice: on June 30 and December 31.

Deployment of the Sentinel compliance tool continued in 2010. This automated tool is now operational for all liquid market investment activities. For the Private Equity and Real Estate portfolios, the Sentinel implementation will begin in 2011.

Finally, significant work was done in 2010 following the adoption of new investment policies for the specialized portfolios. This work aimed to review the tools in place for tracking new limits in all portfolios and implemented a rigorous monitoring system to avoid the breaching of limits.

## CODE OF ETHICS & PROFESSIONAL CONDUCT

All Caisse officers and employees must comply with the Code of Ethics & Professional Conduct. This code aims to emphasize the importance of adopting appropriate behaviour, taking into account the organization's practices, respect for individuals and groups, and compliance with the laws, policies and regulations applicable to the Caisse.

A process in place ensures that all employees annually reconfirm their adherence to the Code of Ethics & Professional Conduct. Furthermore, all employees must report any situation that reasonably appears to represent a breach of the Code.

The Code also includes a pre-approval process for personal employee transactions. Executive Committee members must either place the management of their portfolio in a blind trust or use a passive investment vehicle for corporate securities.

During 2010, the Caisse's practices in this area were compared to those of its peers. This benchmarking confirmed that the Caisse has adopted the best practices in ethics.

The Code of Ethics & Professional Conduct may be consulted on [www.lacaisse.com](http://www.lacaisse.com), under the "Governance" tab.

## Compliance

### INFORMATION ACCESS

The Caisse adopted a policy that defines how it processes and discloses information about itself. It aims to strike a balance between its commitment to transparency and its obligation to protect depositors' interests, while complying with the law and respecting its contractual supplier obligations and third party rights. It also created an "Information Disclosure" section on its website for the documents and information described in Section III of the Regulation respecting the distribution of information and the protection of personal information (R.S.Q. c. A-2.1, r.0.2), where applicable.

In addition, it handles requests for access to documents under the Act respecting access to documents held by public bodies and the protection of personal information (Access Act). During 2010, the Caisse processed 55 document access requests within the legally prescribed period. Out of these 55 requests, 23 were accepted, 22 were accepted in part, 8 were refused, 1 was referred to another body and 1 was abandoned. Only one refused request was subject to an application for review by the Commission d'accès à l'information.

These requests were mainly for documents on the Caisse's investment activities, interaction with depositors and vendors and officer compensation and expense accounts. In cases where a denial was sent, it was for information subject to restrictions on the right of access under the Access Act (Section II of Chapter I of the Act) or personal information (Section I of Chapter III of the Act).

### COMPLAINT MANAGEMENT

The Caisse appointed Ginette Depelteau, Senior Vice-President, Policies and Compliance, to receive, analyze and duly handle complaints. All complaints can be forwarded to her by phone (514-847-5901), fax (514-847-5445) or e-mail ([complaintmanagement@lacaisse.com](mailto:complaintmanagement@lacaisse.com)).

# Contribution to Québec Economic Development

## The Caisse in Québec... a Few Key Numbers

**\$36.5 B**

TOTAL ASSETS  
IN QUÉBEC

**\$3.0 B**

INCREASE IN TOTAL  
ASSETS IN QUÉBEC

**\$20.5 B**

TOTAL ASSETS IN  
QUÉBEC PRIVATE  
SECTOR

**\$1.7 B**

NEW INVESTMENTS  
AND COMMITMENTS  
IN QUÉBEC COMPANIES

**1<sup>st</sup>**

QUÉBEC COMPANY  
PARTNER FOR  
LONG-TERM FINANCING

**500**

PARTNER OF NEARLY  
500 QUÉBEC COMPANIES

**THE CAISSE: ONE OF THE LARGEST  
REAL ESTATE INVESTORS IN QUÉBEC**

---

**293**

OFFICE BUILDINGS  
AND BUSINESS PARKS

**500**

BUILDINGS

**130**

SHOPPING  
CENTRES

**77**

MULTIRESIDENTIAL  
BUILDINGS AND  
HOTELS

## THE CAISSE'S COMPARATIVE ADVANTAGES

- ✓ IN-DEPTH  
KNOWLEDGE  
OF QUÉBEC
- ✓ LONG-TERM  
INVESTOR ROLE

- ✓ CRITICAL MASS
- ✓ INTERNATIONAL  
REACH

### A FIRM COMMITMENT AND CONCRETE ACTIONS IN QUÉBEC

Through its investments, the Caisse aims to generate returns for its depositors and contribute to Québec business and economic growth. For the Caisse, these two fundamental components of its mission go hand in hand, allowing it to best serve the interests of its depositors, Québec companies and Québec.

In fact, the Caisse is a leading institutional investor in Québec. An investor who defines itself as a long-term partner for high-quality, well-managed and promising companies. In addition to providing financing to these companies, the Caisse supports their development on many other fronts, most notably through its global market expertise and network of international partners.

In 2010, the Caisse reaffirmed its commitment to increasing its presence and play its role as a leader in Québec. This resulted in the launch of an action plan with concrete fallout, based on the institution's comparative advantages and supported by its Québec economic development contribution statement.

#### The Caisse's Québec action plan

Guided by common sense and relying on its comparative advantages, the Caisse has begun implementing, step by step, its action plan in Québec. It aims to increase its investments, support local and international growth projects of profitable companies, play its leadership role with the university and financial communities, and continue its efforts to purchase Québec goods and services and promote sustainable development.

In executing its action plan, the Caisse will continue to favour the partnership approach that has characterized its business model, particularly by working closely with companies, universities and other financial players in Québec.

#### An action-oriented structure

To carry out the initiatives of this plan, the Caisse's senior management team established a senior-level Coordination Committee. Working teams composed of representatives from every business unit were also established to coordinate initiatives related to investments, university relationships and the purchase of goods and services. Finally, a Québec business development team has the mandate to broaden the presence of investment teams in the field.

**THE CAISSE IS DETERMINED  
TO GO TO THE EXTENT OF ITS ABILITIES  
TO BETTER SERVE ITS DEPOSITORS,  
QUÉBEC COMPANIES AND QUÉBEC.**

## Contribution to Québec Economic Development

### STATEMENT OF THE CAISSE'S CONTRIBUTION TO QUÉBEC ECONOMIC DEVELOPMENT

The Caisse de dépôt et placement du Québec's mission is to receive moneys on deposit as provided by law and manage them with a view to achieving optimal return within the framework of depositors' investment policies, while at the same time contributing to Québec's economic development.

Returns and economic development go hand in hand. The Caisse aims to use its capacities to the fullest extent to advance Québec's economic development. This is built upon our leadership role in Québec entrepreneurship – through investments in profitable companies that can generate attractive returns for our depositors.

Supported by the overall performance of these financed companies, this contribution also includes supporting their growth, strengthening Québec's financial markets and optimizing our operating expenses in Québec.

Its proximity to and deep knowledge of Québec, its ability as a long-term investor, its critical mass and its international reach represent comparative advantages for the Caisse de dépôt et placement du Québec, offering the opportunity to renew and focus its commitment on the following priorities:

#### 1. Seek and seize the best business and investment opportunities

Invest in funds and support profitable companies with a long-term economic development view, while generating a return that allows our depositors to fulfill their obligations.

- Identify and make profitable, long-term investments in areas we know well.
- Invest in Québec medium-sized firms with the potential to become larger companies.
- Build institutional partnerships to provide companies across Québec with diverse expertise, enhanced services and financial tools.

#### 2. Serve as a bridge to world markets

Offer our diverse expertise, networks and investments to Québec companies that can seize international business opportunities to increase their global presence and accelerate their growth.

- Maximize our presence, networks and level of expertise in all major markets.
- Invest in Québec companies, supporting their efforts to develop new products, enhance their global expansion and accelerate their growth.
- Strengthen strategic partnerships with global institutional investors, while integrating them into our initiatives to strengthen our financial expertise.

#### 3. Contribute to Québec's financial expertise

Draw on the diversity and breadth of all our business units to strengthen the expertise and role of the Caisse as a financial integrator, share our knowledge and increase our presence in Québec communities.

- Support structural initiatives to further dynamize the Québec financial industry.
- Implement development initiatives to enhance financial expertise and nurture the next generation – with universities and other partners.
- Support the development of expertise in responsible investment and sustainable development.

# The Caisse's Achievements in Québec

## HIGHLIGHTS

**01** In 2010, the Caisse's total assets in Québec increased by \$3.0 billion to \$36.5 billion.

**02** Total assets in Québec private sector increased by \$1.8 billion in 2010, reaching \$20.5 billion by the end of the year.

**03** The Caisse has increased its investments in publicly-traded Québec companies by over \$800 million since 2009.

## 1. SEEK AND SEIZE THE BEST BUSINESS AND INVESTMENT OPPORTUNITIES

### INVEST IN AREAS WE KNOW WELL

In 2010, keen to increase its contribution to the Québec economy, the Caisse made many investments by leveraging its comparative advantages, including its knowledge of the Québec business environment and market.

The Caisse provides significant support to companies, typically at a crucial stage of their development, such as part of an expansion or acquisition project. Currently, almost 500 Québec businesses benefit from this support.

#### The Caisse's total assets in Québec

The Caisse's total assets in Québec were \$36.5 billion as at December 31, 2010, up \$3.0 billion from the end of last year.

Table 38 shows the breakdown of total assets in the three major categories of the new portfolio offering for depositors. Please refer to the "Changes in the Portfolio Offering" section on page 23 for more information. The 2009 figures in Tables 38, 39, 40 and 42 also reflect this new classification.

To facilitate understanding of the nature of the Caisse's investments in Québec, Table 39 presents the Caisse's total assets by investment type: government and corporate bonds, publicly-traded company securities, Private Equity group investments and Real Estate group investments. In 2010, total assets increased in each of these categories.

In the private sector, the Caisse is a long-term partner of choice for Québec companies. As a result, the total assets in this sector amounted to \$20.5 billion at the end of 2010, an increase of \$1.8 billion compared to 2009. This proportion of total assets in the private sector demonstrates the Caisse's commitment to Québec companies, which are the engine of economic growth and job creation.

TABLE 38

### CAISSE TOTAL ASSETS IN QUÉBEC

(as at December 31 - in billions of dollars)

	2010	2009
Fixed income	21.8	21.6
Inflation-sensitive investments	5.2	4.5
Equity	9.5	7.4
<b>Total</b>	<b>36.5</b>	<b>33.5</b>

TABLE 39

### CAISSE TOTAL ASSETS IN QUÉBEC

(as at December 31 - in billions of dollars)

	2010	2009
Bonds	22.8	22.1
Equity Markets	2.7	2.1
Private Equity group	4.2	3.4
Real Estate group	6.8	5.9
<b>Total</b>	<b>36.5</b>	<b>33.5</b>
Private sector	20.5	18.7
Public sector	16.0	14.8
<b>Total</b>	<b>36.5</b>	<b>33.5</b>

## The Caisse's Achievements in Québec

### Bonds: A \$700 million increase in assets

The Caisse's total bond assets in Québec's public and private sectors amounted to \$22.8 billion as at December 31, 2010, up \$700 million over the previous year. The Caisse is one of the largest holders of government bonds in Québec, with a portfolio of close to \$9 billion, a \$1.0 billion increase compared to 2009 (see Table 40).

At the height of the 2009 liquidity crisis, when access to financing was more difficult, the Caisse issued large loans to many Québec companies. Market conditions have since greatly improved – certain companies have benefited from a significant level of liquidity and repaid part or all of their loans. This situation partly explains the slight decrease in 2010 total Québec private sector bond assets.

Moreover, in 2010 the Caisse renewed the loans of several Québec companies in the portfolio, such as Garda World Security Corporation and TransForce.

### GARDA

With the Caisse's support, Garda World Security Corporation refinanced its debt in 2010. Garda is one of the world's most renowned investigative, consulting and security companies. The refinancing allowed the firm to improve its financial structure and provided greater flexibility for future growth.

TABLE 40

### ASSETS IN QUÉBEC – BONDS

(as at December 31 – in billions of dollars)

	2010	2009
<b>Québec public sector</b>		
Québec government	9.0	8.0
Hydro-Québec	4.4	4.2
Other state-owned enterprises	1.6	1.5
Municipalities and para-governmental corporations	1.0	1.1
<b>Subtotal</b>	<b>16.0</b>	<b>14.8</b>
<b>Private sector: corporate securities</b>	<b>6.8</b>	<b>7.3</b>
<b>Total</b>	<b>22.8</b>	<b>22.1</b>

### TRANSFORCE

The Caisse also invested in TransForce, a leader in Canada's transportation and logistics sectors. In 2010, a financial syndicate that included the Caisse has undertaken to grant the company a credit facility of \$650 million to refinance its existing bank debt.

### Equity markets: An increase in the Caisse's support of Québec publicly-traded companies

As at December 31, 2010, the Canadian Equity portfolio's assets in Québec companies amounted to \$2.7 billion, representing an increase of \$600 million compared to 2009.

This increase reflects, for instance, the willingness of the Caisse to leverage even more on its comparative advantage in proximity and close relationships with local companies, which translates into in-depth knowledge of the Québec market. In late 2010, the Caisse held 45 Québec companies in the portfolio, five of which were new investments.

Table 41 presents the Top 10 publicly-traded Québec company positions.

In March 2011, the Caisse also announced that, since late 2009, it has increased its investments in publicly-traded Québec companies by \$800 million.

The new National Bank Québec Index™, dedicated exclusively to Québec-based companies, was also included in the Canadian Equity portfolio's benchmark index. The latter is now much more representative of the composition of the portfolio and better reflects Québec's weight in the Canadian economy, which is about 20%, compared to Québec-based companies which account for approximately 10% of the S&P/TSX index. The Canadian Equity portfolio's benchmark index is now composed of 90% of the S&P/TSX index and 10% of the National Bank Québec Index™.

### D-BOX

In 2010, the Caisse invested \$7.1 million in shares and warrants in the company D-Box to support its international activities. D-Box is a global leader in motion systems, mainly for the film industry. It is particularly known for its seats that create motion synchronized with onscreen action. D-Box also collaborates with many of the largest studios in the industry.

TABLE 41

### TOP 10 POSITIONS – EQUITY MARKETS

(as at December 31, 2010)

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Astral Media Inc
Bombardier Inc
Canadian National Railway Company
CGI Group Inc
Consolidated Thompson Iron Mines Limited
Gildan Activewear Inc
National Bank of Canada
Power Corporation of Canada
RONA Inc
SNC-Lavalin Group Inc

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## The Caisse's Achievements in Québec

### An \$870 million increase in Private Equity group assets

The Caisse invests in private equity, directly and through funds, in over 400 Québec companies. Its Private Equity group manages the Infrastructure and Private Equity portfolios.

Private equity is negotiated by mutual agreement with companies. The Caisse is recognized for its vast 30 year expertise in this area.

### GREATER INVESTMENT IN GAZ MÉTRO

The Caisse has maintained a profitable business relationship with Gaz Métro for many years. In recent months, it substantially increased its investment in this company, which is active in Québec, Canada and the northeastern portion of North America, particularly in the distribution and transportation of natural gas. The Caisse believes that Gaz Métro possesses the strengths to maintain its current leadership position. With Gaz Métro, the Caisse has a high-quality investment that provides consistent returns to its depositors and the Québec economy.

The Caisse increased its stake in the company by acquiring additional interests in Trencap and Noverco, two companies linked to Gaz Métro. These two transactions could represent an investment of over \$300 million.

Private equity assets in Québec amounted to \$4.2 billion as at December 31, 2010, an increase of nearly \$870 million compared to 2009. Table 43 presents the Top 10 private equity positions in Québec.

In 2010, the Caisse approved more than 10 new investments totalling \$680 million. In addition to the significant increase in its Gaz Métro stake, it invested in several funds and medium-sized companies. For example, it reinvested \$10 million in Sodemex, a limited partnership with a portfolio of \$95 million invested in 61 small-cap companies in the Québec mining sector. The Caisse also supported again Mechronix, a leader in the flight simulator industry, with an investment of \$4.4 million.

The Caisse acquires stakes in strong Québec companies with excellent growth potential. This partly explains the increase in value of its investments in 2010.

TABLE 43

### TOP 10 QUÉBEC INVESTMENTS – PRIVATE EQUITY GROUP

(as at December 31, 2010)

Alterinvest II Fund L.P.
Camoplast Inc
Domtar Corp
Fiera Axiom Infrastructure Canada LP
GLV Inc
J.A. Bombardier (J.A.B.) Inc
Noverco Inc. (Gaz Métro)
Quebecor Media Inc
SSQ Vie
Yellow Media Inc.

TABLE 42

### PRIVATE EQUITY GROUP ASSETS AND COMMITMENTS IN QUÉBEC

(as at December 31 – in millions of dollars)

	2010			2009		
	Assets	Undisbursed commitments	Assets and undisbursed commitments	Assets	Undisbursed commitments	Assets and undisbursed commitments
Venture capital	104	341	445	111	366	477
Small and medium-sized businesses	420	489	909	378	594	972
Large businesses	3,731	525	4,256	2,897	32	2,929
<b>Total</b>	<b>4,255</b>	<b>1,355</b>	<b>5,610</b>	<b>3,386</b>	<b>992</b>	<b>4,378</b>

### Real Estate group: A dynamic unit with high-quality assets

The Caisse is well established in Québec's real estate sector. Its Real Estate Group, which manages the Real Estate Debt and Real Estate portfolios, is a major investor in Québec in this market, with total assets amounting to \$6.8 billion as at December 31, 2010, an increase of over \$870 million compared to 2009 (see Table 44).

Around forty new investments were authorized in this sector during the year, totaling close to \$750 million. At the end of 2010, the Caisse owned nearly 70 buildings and was financing more than 430 commercial real estate properties in Québec.

The Caisse's real estate assets benefited from improved market conditions, particularly in the retail sector. The Real Estate Debt portfolio also profited from a more vibrant market, particularly in the office building sector.

Through their Québec investment activities, the Caisse's real estate subsidiaries target high-quality buildings with an excellent location in their market. The quality of this real estate portfolio is reflected in the Caisse's 95% occupancy rate in 2010. Table 45 presents the Top 10 real estate investments in Québec.

Each year, as part of its real estate activities, the Caisse also invests heavily in repositioning and renovating its properties. In 2010, this represented an injection of nearly \$40 million by the Caisse in the Québec economy.

TABLE 45

### TOP 10 QUÉBEC INVESTMENTS – REAL ESTATE GROUP

(as at December 31, 2010)

1000 De La Gauchetière Ouest, Montréal
Centre CDP Capital, Montréal
Centre Eaton de Montréal, Montréal
Fairview Pointe-Claire, Montréal
Galeries d'Anjou, Montréal
Laurier Québec, Québec
Place Ville Marie, Montréal
Rockland, Montréal
Place Ste-Foy, Québec
World Trade Centre Montréal, Montréal

### PLACE STE-FOY

In 2010, Ivanhoe Cambridge completed its \$50 million renovation and expansion of Place Ste-Foy which started in January 2008. This project aimed to expand and renovate La Maison Simons. With a leasable area of approximately 637,000 square feet, Place Ste-Foy has more than 135 boutiques and stores.

### LAURIER QUÉBEC

In 2010, Ivanhoe Cambridge acquired a 50% stake held by OMERS in Laurier Québec, becoming the owner of the entire building, with an investment of \$200 million. This mall is the largest in Eastern Canada, with over 1.2 million square feet of space and 350 stores.

TABLE 44

### REAL ESTATE GROUP ASSETS AND COMMITMENTS IN QUÉBEC

(as at December 31 – in millions of dollars)

	2010			2009		
	Assets	Undisbursed commitments	Assets and undisbursed commitments	Assets	Undisbursed commitments	Assets and undisbursed commitments
Office	2,951	214	3,165	2,295	2	2,297
Retail	3,136	41	3,177	2,793	55	2,848
Other assets	689	18	707	818	130	948
<b>Total</b>	<b>6,776</b>	<b>273</b>	<b>7,049</b>	<b>5,906</b>	<b>187</b>	<b>6,093</b>

## The Caisse's Achievements in Québec

### INVESTING IN QUÉBEC SMBs WITH THE POTENTIAL TO BECOME LARGE INTERNATIONAL COMPANIES

Currently, only 30% of Québec small and medium-sized businesses (SMBs) export to Europe, and only 16% to Asia. Given the limited size of the Québec and Canadian economies, Québec-based companies must expand into international markets to continue growing.

The Caisse estimates that there are dozens small and medium-sized businesses in Québec with the capacity to become major global companies. Its goal is to invest in the best of them – not only to contribute to Québec's economic development, but also to seize profitable business opportunities.

### GRAHAM GROUP INTERNATIONAL

As part of its partnership with Desjardins, the Caisse invested up to \$7.2 million in Graham Group International (GGI), a family business specializing in the design, engineering and manufacture of user interface assemblies for advanced sectors such as aeronautics and telecommunications. Financial support from the Caisse and Capital régional et coopératif Desjardins will enable the company to keep its control in Québec and promote its expertise and products worldwide.

### TWO INVESTMENTS OF THE QUÉBEC MANUFACTURING FUND

Created in 2009, the Québec Manufacturing Fund (QMF) combines the financial expertise of the Caisse and the operational skills of experienced managers to identify profitable Québec manufacturing company that represent investment opportunities. With \$100 million in capital and the Caisse's sponsorship, in 2010 the QMF invested in two medium-sized companies with strong potential.

#### HASON STEEL PRODUCTS

The QMF invested \$4 million in Hason Steel Products Inc., a leading North American manufacturer of catalytic cracking unit components for crude oil refineries. The company, which has nearly 150 employees at its plants in Lanoraie and Berthierville, sells its products in the Americas, Asia, Middle East and Europe. QMF's support enabled Hason to expand its Lanoraie plant, improve productivity and continue its expansion into international markets.

#### AVANT-GARDE TECHNOLOGIE

In December 2010, QMF invested \$3 million in Avant-Garde Technologie (AGT), a company that designs, develops and delivers customized automated solutions to improve the operational efficiency of manufacturing companies. This financial support will enable the company to acquire Orus Intégration, which specializes in artificial vision, and become an automation solution leader in Québec. It also allowed the firm to continue its efforts to develop and commercialize a unit for the automated manufacturing of steel structures.

### FORGING PARTNERSHIPS WITH OTHER INSTITUTIONS TO ENHANCE OUR SUPPORT FOR COMPANIES

Promising SMBs are everywhere throughout Québec. To ensure that these companies have access to its expertise and its financial resources, the Caisse partnered with Desjardins Group, a financial institution highly integrated into the social and economic fabric of Québec.

This three-year \$600 million agreement has two components. The first part of the agreement involves a \$200-million fund, called Capital Croissance PME, for meeting the financing needs of small companies, primarily in the form of subordinated loans of less than \$3 million. The second part of the agreement involves \$400 million for the financing of medium-sized companies, primarily through conventional term loans of over \$5 million and in the form of equity and quasi-equity.

In 2010, \$62 million in investments were authorized under this partnership. This money will enable nearly a dozen firms in eight Québec regions to increase their productivity, carry out their growth projects and, in turn, maintain their industry leadership positions.

### COMPANIES SUPPORTED BY THE PARTNERSHIP WITH DESJARDINS GROUP

---

AMBULANCE MÉDILAC INC.  
Métabetchouan,  
Saguenay-Lac-Saint-Jean

CAN-LAK  
Daveluyville,  
Centre-du-Québec

GROUPE FILION SPORTS  
Rimouski,  
Bas-Saint-Laurent

GRAHAM INTERNATIONAL  
GROUP INC.  
Montréal

GROUPE LOISELLE  
Salaberry-de-Valleyfield,  
Montréal

SID LEE  
Montréal

PROGI-PAC GROUP  
Trois-Rivières,  
Mauricie

STC FOOTWEAR INC.  
Montréal

LOCATION PAUL BOUDREAU  
Havre-Saint-Pierre,  
Côte-Nord

LUCIEN MIRAULT INC.  
Val d'Or,  
Abitibi

SYSTEMEX  
Montréal

## The Caisse's Achievements in Québec

### 2. SERVE AS A BRIDGE BETWEEN QUÉBEC COMPANIES AND WORLD MARKETS

For the Caisse, Québec economic growth and wealth creation are largely based on the ability of Québec companies to carve out a niche in global markets and increase their exports.

Today and tomorrow, competition and business opportunities will come from every corner of the planet. Québec has the ability to meet this challenge and seize these opportunities. And the Caisse can play a major role as a bridge for Québec companies with the ability to conquer global markets. This is the part of its strategy that the Caisse intends to broaden in coming years.

#### INVESTING IN QUÉBEC COMPANIES TO ENHANCE THEIR INTERNATIONAL EXPANSION

The Caisse offers its international reach, investments in world markets, global business networks and new market expertise to promising Québec companies. Its goal: support growth projects of these companies to help make them champions on the world stage – for the benefit of Québec.

This "Bridge to the World" vision will not only be achieved through investments, but also by organizing discussion forums on best practices related to the challenges of globalization.

#### "DIALOGUES" CONFERENCES

To further support the international efforts of Québec companies, the Caisse organized four "Dialogues" conferences in 2010 in Lévis, Saguenay, Drummondville and Montréal. These expert-led workshops are held for the heads of SMBs, offering them a forum for sharing their experiences on various topics related to the challenges of globalization: adapting their business models, managing their human resources and leveraging their information technology. In the past year these conferences have attracted more than 400 participants. In total, seven "Dialogues" seminars have been held since their launch in 2009. These conferences will continue in 2011 in other Québec cities.

#### BSA

In November 2010, the Caisse invested \$7.8 million in BSA, a leader in technical services for the food and meat processing industry in Québec, Atlantic Provinces and Ontario. BSA is a dominant player in its sector with good growth potential. Founded in 1989, it has 135 employees, including 120 in Québec. Its activities are divided into four divisions, one of which is located in India. Support from the Caisse will for instance enable BSA to carry out its expansion plans abroad.

#### CIRQUE DU SOLEIL

The Caisse is a long-time partner of Cirque du Soleil, a Québec company recognized internationally for its shows and high-quality artistic entertainment – and whose international head office is in Montréal. Already in 2001, the Caisse had contributed \$50 million of a \$250 million financing, enabling the founders to redesign their partnership structure. In 2010, the Caisse authorized a \$25 million investment to support Cirque's international expansion. This investment project involves two new shows that will be held in Los Angeles, New York and Moscow.

#### FORGING PARTNERSHIPS WITH INSTITUTIONAL INVESTORS WORLDWIDE

The Caisse aims to use its critical mass, global reach and credibility in international markets to further expand its networks throughout the world, particularly in emerging countries. That's why it established two significant partnerships with institutions well positioned in the global arena.

#### A new partnership with HSBC Bank, a global financial institution with a significant presence in Asia and Brazil

Québec medium-sized companies face many obstacles on the path to international expansion, whether their plans involve acquiring a competitor or promoting their activities abroad. Recognizing these challenges, the Caisse and HSBC Bank Canada joined forces in late 2010 to create a financing solution for international investment projects. The complementarity of their financing and services offering, coupled with their vast network, represents truly unique support for Québec companies.

**The partnership with AXA Private Equity, formed in 2009, is starting to bear fruit**

Québec companies are seeking not only financing but also business opportunities abroad. Access to an extensive and solid network is crucial for entrepreneurs. In 2009, the Caisse and AXA Private Equity, a company with activities in Europe and Asia, therefore decided to share their respective networks. Since then, nearly 40 companies in Québec and Europe have benefited from networking opportunities on both sides of the Atlantic. For instance, this agreement has allowed a Québec company specializing in industrial piping to offer its services as a supplier of a large European customer order. Another Québec company and a European SMB, specializing in project management solutions, were able to discuss their challenges and develop a common strategy for conquering their respective markets.

**FINANCE MONTRÉAL**

The Caisse also contributes to the financial industry by supporting structural initiatives. In 2010, it joined and actively participated in Finance Montréal, Québec's new financial cluster. It supports the commitment of this organization to strengthen the province's financial sector, initiate new business activities, encourage business creation and attract international companies to Québec.

**3. CONTRIBUTE TO QUÉBEC'S FINANCIAL EXPERTISE**

The Caisse's contribution does not only come from its financial investments. The volume and scope of its activities also make the Caisse a financial integrator in Québec. It is active, directly and indirectly, in every profession related to finance. This critical mass contributes to maintain an active and modern Québec financial community, which will become a catalyst for economic development and growth.

**SUPPORTING INITIATIVES THAT DRIVE QUÉBEC'S FINANCIAL INDUSTRY**

The Caisse's contribution to Québec financial industry may be measured in different ways. For example, it should be noted that of the \$3 billion in banking operations that it carries out daily, more than two thirds are processed through banks and brokers established in Québec.

In addition, the Caisse can attract foreign companies, generating economic activity and creating employment in Québec. This approach was taken in 2009 with a French supplier, which produces computer applications for the financial sector. The company now employs 10 people in Montréal. For many years, the Caisse has used the services of Québec asset management providers that stand out due to their comparative advantages, including Van Berkorn & Associates, Hexavest, Crystalline/Amethyst, HRStratégies and AFC. It is also in the process of concluding further such agreements.

In a different vein, the Caisse and its real estate subsidiaries annually spend nearly \$600 million in Québec, including almost \$400 million for real estate operating expenses alone. More than 1,800 Québec suppliers are called upon to fill the needs of these business activities, contributing to the creation or maintenance of many jobs in the province - not to mention the impact on financial expertise development. The Caisse's Policy on Contracts for the Acquisition or Leasing of Goods and Services also facilitates the institution's contribution to economic development and sustainable development. This policy aims to promote Québec suppliers, provided they meet the Caisse's cost and quality criteria.

## The Caisse's Achievements in Québec

### IN COOPERATION WITH UNIVERSITIES AND OTHER PARTNERS, LAUNCH INITIATIVES TO ENHANCE OUR FINANCIAL EXPERTISE AND NURTURE THE NEXT GENERATION

Human capital is essential for creating an environment favourable to a dynamic financial industry. In this area, talent comes first. The Caisse believes that the industry must continue to invest in the development of a large pool of financial expertise. The Caisse will also be proactive and share its knowledge and expertise, by strengthening its ties with universities.

Partnerships with universities, particularly business schools, are vital to the Caisse's commitment. In the fall of 2010, three internal working groups (applied research, talent acquisition and expertise development) developed and began implementing a number of major initiatives.

Here's a preview of the first initiatives in 2010:

- Tour of Québec universities to establish new collaboration methods.
- Presentations by the Caisse's experts in university courses to introduce students to career opportunities in finance.
- Applied research agenda with several universities, allowing the Caisse to guide the work of researchers on strategic issues, while offering them the opportunity to use its expertise and network.
- Internship program at the Caisse to expose university students to highly specialized finance careers paths.
- 13th annual HEC Montréal Undergraduate Stock Exchange (SBIU) hosted by the Caisse in collaboration with SITQ and CGI.
- Partnership with the École d'entrepreneurship de Beauce (ÉEB), a unique institution dedicated to training the next generation of entrepreneurs.

### SUPPORTING THE DEVELOPMENT OF RESPONSIBLE INVESTMENT AND SUSTAINABLE DEVELOPMENT EXPERTISE

The Caisse's contribution to Québec financial industry also partly stems from the development of its responsible investment expertise. In a spirit of continuous improvement, investment strategy simplification and optimal risk management, the Caisse updated its Policy on Responsible Investment, which has been in effect since 2005. This update, conducted in 2010, incorporates the Caisse's experience and industry trends in responsible investing. See pages 86-91 for more details on this policy.

The Caisse and its real estate subsidiaries have been committed to sustainable development for many years. Their actions in this area target and enhance the social, economic and environmental impact of their activities. In 2009, the Caisse released its first Sustainable Development Action Plan, which covers its efforts for the 2009-2011 period. The plan is based on best practices and is aligned with the objectives defined in Québec's Sustainable Development Act. The progress of the Caisse's Sustainable Development Action Plan can be found in the "Sustainable Development Report" section on pages 80 to 84.

### SURVEY ON INTEGRATION OF SUSTAINABLE DEVELOPMENT PRINCIPLES

In 2010, with financial support from the Caisse, the Fondation de l'entrepreneurship created the Québec Entrepreneurial Index in collaboration with Léger Marketing. This index includes many results on the integration of sustainable development principles by Québec entrepreneurs. The survey is the first in Québec to explore the topic – from the standpoint of the entrepreneur, not the company. The results show a mindset shift toward the integration of sustainable development principles into business management.

### **Donations and sponsorships to benefit Québec communities**

Each year, as a responsible corporate citizen, the Caisse provides financial support to organizations whose mission is to contribute to the betterment of the business community and the community at large. This contribution mainly takes the form of donations and sponsorships. In 2010, the Caisse made nearly \$1.9 million in contributions to various organizations and events.

In line with its Policy on donations and sponsorships, the Caisse earmarks most of its funds to issues related to business leadership, tomorrow's financial professionals and knowledge development. Here are examples of projects that the Caisse supported in 2010:

- **Fédération des chambres de commerce du Québec:** Meetings in several Québec cities enabled the Caisse's managers to better understand the needs and challenges faced by entrepreneurs in the region.
- **Collège des administrateurs de société:** This organization's courses take place at the Caisse's headquarters in Québec. Supported by the Caisse, the Collège continues its activities, seeking to be the centre of excellence for corporate director training and the benchmark for governance.
- **Québec manufacturers and exporters:** Seminars on operational efficiency and productivity have been organized for members of this organization by the Québec Manufacturing Fund.

The Caisse also participated in various discussions about world market conditions and challenges facing Québec companies, such as "Focus stratégique" and the "Tournée des régions Les Affaires" on business transfers.

Finally, the Caisse and its real estate subsidiaries supported their employees' Centraide fundraising campaign.

### **"EXPORTING QUÉBEC – SMALL BUSINESS CONQUERING THE WORLD" INITIATIVE**

The Caisse is actively involved in various initiatives that help businesses better face the challenges of internationalization. For this reason, it contributes to the "Exporting Québec – Small business conquering the world" initiative of the World Trade Centre Montréal, which aims to educate Québec companies about international business opportunities.

### **THE PROSPERITY PROJECT**

As a partner of Groupement des chefs d'entreprise du Québec for many years, the Caisse renewed its three-year support of the Prosperity project in 2010. This unique initiative stems from the commitment of the Groupement's entrepreneurs, from eight financial institutions and the Québec government. This project will foster greater collaboration between entrepreneurs, financial institutions and governments, promoting business growth and creating greater prosperity in Québec.

# Sustainable Development Report

## HIGHLIGHTS

**01** In 2010, the Caisse submitted an implementation report on the Equal Access to Employment program.

**02** In April 2010, Caisse held a Sustainable Development Week to educate its employees about its approach.

**03** The 2010 employee fundraising campaign for the benefit of Centraide raised \$882,846.

## A THREE-YEAR ACTION PLAN

In 2009, the Caisse released its first Sustainable Development Action Plan, which covers the actions for the 2009-2011 period. The Plan is based on best practices and is secured to the objectives defined in the Sustainable Development Act, R.S.Q. c. D-8.1.1. It includes nine organizational objectives. The institution also established a Sustainable Development Committee comprised of representatives from its various units to oversee the plan's implementation.

The sustainable development concept fits naturally into the Caisse's mission since it affects both the continuity of depositors' funds and Québec's long-term economic development.

## EMPLOYEE AWARENESS AND TRAINING

Since 2009, the Caisse has carried out an ongoing awareness program to encourage employees to behave in accordance with sustainable development principles at work and at home.

In 2010, the Caisse held a Sustainable Development Awareness Week for its employees. In addition, it has various tools at its disposal, including a Green Guide that lists four types of green practices to adopt: recycle, reuse, reduce and rethink.

In the coming years, the Caisse aims to continue playing its role in sustainable development. This Action Plan outlines the key initiatives conducted in 2010. It also presents the actions carried out in 2009 and planned for 2011 (see Table 46).

TABLE 46

## CAISSE SUSTAINABLE DEVELOPMENT ACTION PLAN STATUS

### Organizational objective

Promote the sustainable development initiatives of the Caisse and its real estate subsidiaries.

### ACTION 01

	Milestones	Initiatives
Present the sustainable development concept and principles to the Caisse's stakeholders (such as the general public, depositors, tenants, etc.)	2009	Publication of a responsible investment (RI) report.
	2010	Steps were taken to identify and categorize all the corporate social responsibility (CSR) work and actions of the Caisse and its subsidiaries. The Caisse also developed a new section on its website dedicated to its sustainable development and social responsibility activities. The next step: the Caisse will publish a corporate social responsibility (CSR) report in 2011.
	Future	<b>2011</b> – Seminar on responsible investment and sustainable development for depositors.

TABLE 46

**Organizational objective**

Promote the sustainable development initiatives of the Caisse and its real estate subsidiaries.

**ACTION 02**

	Milestones	Initiatives
Implement activities that help achieve the Government Plan for public sector personnel awareness and training	2009	<p>Awareness of sustainable development through the employee newsletter <i>Scoop</i> (publication of three articles and two Eco-Caisse capsules).</p> <p>Conference program in 2009: 536 participants over eight sessions.</p>
	2010	<p>Employee participation in training by the Ministère du Développement durable, de l'Environnement et des Parcs.</p> <p>Development of a plan for portfolio manager training on responsible investment.</p> <p>Sustainable Development Week (April 19-23, 2010) for employees with many awareness activities, including lunch with representatives of Équiterre and Québec companies, information stands on more responsible consumption tips and ideas, as well as used bicycle, book and non-perishable food collections.</p> <p>Presentation of the Sustainable Development Action Plan at orientation sessions for new employees.</p> <p>Sustainable development awareness through an internal newsletter, Employee Green Guide and Éco-Caisse capsules on the Intranet.</p> <p>Continued internal conference program established in 2009: 450 participants over five sessions.</p>
	Future	<b>2011</b> – Responsible investment training for portfolio managers.

## Sustainable Development Report

TABLE 46

### Organizational objective

Contribute to the discussion on sustainable development.

### ACTION 03

	Milestones	Initiatives
Participate in sustainable development events and groups	2010	Creation of a discussion group bringing together stakeholders from government bodies responsible for sustainable development to discuss actions and initiatives of each organization and see whether to establish a partnership for joint action. The meetings will continue in 2011.

### Organizational objective

Establish working conditions conducive to employee health and safety.

### ACTION 04

	Milestones	Initiatives
Invest in risk prevention to ensure employee health and safety	2009	Creation of a prevention committee (meeting held in December), composed of employees from all Caisse units.
	2010	Committee meetings on workplace prevention, which encouraged the Caisse to reconsider the location of printers and endorse decisions about replacing water dispensers with water coolers and composting paper towels in the restrooms.  Implementation of employee safety programs.

### Organizational objective

Develop responsible procurement practices for goods and services.

### ACTION 05

	Milestones	Initiatives
Implement practices and activities that fulfill eco-responsible government policy provisions	2009	Inclusion of sustainable development criteria in the standard tender document.  Design of the "green office" guide for employees (distributed in December).
	2010	Adoption of the Policy on Contracts for the Acquisition or Leasing of Goods and Services that reflects 16 sustainable development principles.  Implementation of a specific guideline for computer equipment purchases.

TABLE 46

**Organizational objective**

Promote sound environmental management at the Caisse and its real estate subsidiaries.

**ACTION 06**

	Milestones	Initiatives
Implement measures for environmental building management	2009	Maintainance of BOMA BEST certification.
		LEED <sup>1</sup> certification for the Caisse's business office (Centre CDP Capital): September 11, 2009 confirmation.
		LEED certification for a Vancouver building under construction: confirmation of pre-certification pending completion of construction.
		Creation of SITQ Group building tenant committees: first meetings held during the year.

**ACTION 07**

	Milestones	Initiatives
Implement an environmental management system for the Caisse's Montréal business office	2009	Creation of a "Green" committee at Centre CDP Capital, composed mostly of tenants.
	2010	Monitoring of measures related to the Montréal office's ecological footprint to maintain a level of excellence and to reduce its footprint. The monitoring results encompass the amount of consumed waste, water, energy and paper – in addition to the amount of recycled paper and the percentage of recycled waste.
		Development of an environmental management system that will be implemented in 2011. In 2010, all Centre CDP Capital management activities were first analyzed based on key environmental aspects and impacts, then prioritized. Improvement targets were subsequently established.
	Future	<b>2011</b> – In 2010, the Caisse participated in a discussion with its real estate subsidiaries that will lead to the adoption of a policy.

**Organizational objective**

Help protect Québec's cultural heritage.

**ACTION 08**

	Milestones	Initiatives
Promote Québec's cultural heritage	2010	Exhibition of several works of art from the Caisse's collection during summer 2010. This exhibition was accessible to employees and the general public.

1. Leadership in Energy and Environmental Design

## Sustainable Development Report

TABLE 46

### Organizational objective

Increase cooperation with national and international partners on integrated sustainable development projects.

### ACTION 09

	Milestones	Initiatives
Work with a partner on a sustainable development project	2010	A real estate subsidiary activity with Équiterre to promote its mission and participate in its financing activity.
	Future	<b>2011</b> – Establishment of a partnership with depositors on sustainable development matters.

### Organizational objective

Support non-profit organizations that help prevent and fight poverty and social exclusion.

### ACTION 10

	Milestones	Initiatives
Support philanthropic causes	2009	Real estate subsidiary Ivanhoe Cambridge established a permanent volunteer program, Give & Take, to encourage its employees to do volunteer work. It offers two days of paid leave to employees who devote one of the two days to volunteering at a charity of their choice. In 2009, more than 400 employees participated, representing nearly 28% of the subsidiary's workforce.
	2010	An annual fundraising campaign for Centraide.  Development of volunteer program at real estate subsidiaries.
	Future	<b>2011</b> – Development of volunteer program for the Caisse.

### ACTION 11

	Milestones	Initiatives
Implement a company diversity program	2009	Diversity Week (June 1-5, 2009).
	2010	Diversity Week (November 29-December 3, 2010).  Creation of an Equal Access to Employment committee. An Equal Access to Employment program implementation report was tabled.
		Multicultural team management training for team leaders.

# Responsible Investment

# Responsible Investment Report

## HIGHLIGHTS

**01** In 2010, the Caisse updated its Policy on Responsible Investment.

**02** The Caisse exercised its voting rights at 4,388 shareholder meetings.

**03** The Caisse joined CDP (Carbon Disclosure Project) Water Disclosure in January 2011.

## PROACTIVE ENGAGEMENT FOR MANY YEARS

As early as 1994, the Caisse adopted a Policy on the Principles Governing the Exercise of Voting Rights of Public Companies. In January 2005, the Caisse adopted a Policy on Responsible Investment.

In 2006, the Caisse was one of the first signatories of the UN Principles for Responsible Investment (PRI). It became an active member of the Carbon Disclosure Project – Canada Advisory Group, an international initiative that calls for the more accurate measurement and reduction of carbon emissions. In January 2011, the Caisse joined CDP (Carbon Disclosure Project) Water Disclosure, another initiative from the same group.

## EXERCISING OUR INVESTOR ROLE RESPONSIBLY

As one of the largest institutional investors in Canada, the Caisse has many resources at its disposal to influence the social responsibility, environmental and governance practices of companies. This approach takes into account depositors' fund returns and expectations, particularly when it comes to risk and responsible investment.

In 2010, as part of its continuous policy and process improvement, which aims to streamline its investment strategies and improve its risk management practices, the Caisse reviewed its investment policies, including its Policy on Responsible Investment. Specifically, it reviewed its entire approach, benchmarking it against its peers, and assessed the implementation of its policy five years after its adoption. This policy has been updated and is now built around the following key areas.

### 1. Shareholder engagement

The Caisse's shareholder engagement activities are conducted through a proactive dialogue with companies, independently or in collaboration with investor groups, to improve the level of information available to them and influence their responsible business practices. The Caisse will enhance its shareholder engagement efforts with these companies by targeting specific issues recommended by the Responsible Investment Committee – such as governance and natural resource exploitation matters. The Caisse's shareholder engagement activities also include the systematic exercise of its voting rights at shareholder meetings.

### 2. Environmental, social and governance (ESG) criteria

The integration of ESG criteria in portfolio management decisions is entrenched in its Equity Markets group. The Caisse is enhancing the process of integrating these criteria in other asset class decision-making to improve the assessment of all investment-related risks and opportunities.

### 3. Exclusions

Although shareholder dialogue and engagement remain its principal policy tool, the Caisse can, if exceptional circumstances warrant it, exclude from its portfolio the securities of companies in violation of local or international law.

### 4. Responsible Investment Committee

A standing Responsible Investment Committee was established to examine responsible investing issues, structure existing initiatives and develop any new approach that reflects the Caisse's ongoing priorities.

## 2010 RESPONSIBLE INVESTMENT REPORT

This responsible investment report reviews the Caisse's overall activities during 2010 under its Policy on Responsible Investment and its Policy on the Principles Governing the Exercise of Voting Rights of Public Companies.

In addition to revising its Policy on Responsible Investment, the Caisse acted in accordance with the four thrusts of its approach.

### 1. SHAREHOLDER ENGAGEMENT BY EXERCISING VOTING RIGHTS

Each year, the Caisse reviews all proposals tabled at the shareholder meetings of Canadian and U.S. public companies in its portfolios.

Voting rights are exercised by an internal team for the shareholder meetings of Canadian and U.S. companies. For international companies, votes are exercised by an external supplier in accordance with the Caisse's policies and guidelines. All voting positions for Canadian and U.S. companies are published on the Caisse's website: [www.lacaisse.com](http://www.lacaisse.com).

For shareholder meetings of international companies, the internal team ensures that the external supplier exercises the voting rights in accordance with the Caisse's policies.

### 2010 voting report

The following provides the highlights for 2010 regarding the exercise of voting rights.

#### The Caisse voted on 39,470 resolutions at 4,388 shareholder meetings

- Canada: 175 meetings
- United States: 581 meetings
- International: 3,632 meetings

#### Out of the Caisse's total votes in 2010, 12% were against management proposals

- 7%: Canada
- 13%: United States
- 12%: International

### Votes on management proposals

Most shareholder meeting proposals are tabled by the company's management and are connected to the election of directors, as well as the appointment of auditors and other matters that arise in the normal course of business.

Generally, the Caisse supports the recommendations made by management. Sometimes, however, it opposes them. Table 47 presents examples of such opposition.

TABLE 47

### EXAMPLES FOR OPPOSITION

Type of Management Proposals	Number of "Against" Proposals	Reasons
COMPENSATION PROGRAM	Out of 84 proposals, the Caisse voted against management in 37% of the cases.	The compensation is not linked to the company's performance or the stock option plan dilution is too high.
ELECTION OF DIRECTORS	Out of 1,217 director proposals, the Caisse voted against management in 5% of the cases.	Non-independent directors or the director's absenteeism.

## Responsible Investment Report

### Votes on shareholder proposals

Each shareholder proposal at the meetings is reviewed and analyzed on a case-by-case basis. In 2010, the Caisse voted on 487 shareholder proposals at meetings of Canadian and U.S. companies. The Caisse supported 380 of these proposals.

Tables 48 and 49 give examples of shareholder proposals considered by the Caisse in 2010.

## EXAMPLES OF THE CAISSE'S POSITIONS

### Separate vote/majority vote/ Annual election of directors

The Caisse supports the position that allows shareholders to vote for or against individual directors, based on an assessment of their contribution to the Board of Directors – and even remove a director. Annual elections allow shareholders to regularly make their opinions known in this respect.

### Information disclosure

In principle, the Caisse favours the disclosure of information by companies because it allows the institution to better evaluate its investments. It therefore generally supports proposals that seek greater disclosure on environmental, social and governance issues. However, the Caisse votes against these proposals if it believes that the company is already making such disclosure or whenever a required

disclosure exceeds the company's area of responsibility – for example, a matter within the jurisdiction of a government or another authority.

TABLE 48

## TYPES OF SHAREHOLDER PROPOSALS GENERALLY OPPOSED BY THE CAISSE

### PROPOSALS

LIMIT EXECUTIVE  
COMPENSATION

CREATION OF A BOARD COMMITTEE  
ON ENVIRONMENTAL AND  
SOCIAL ISSUES

SCIENTIFIC REPORT ON  
CLIMATE CHANGE

### Reasons for voting against proposal

This measure is arbitrary and does not reflect best practices in the marketplace. The Board should have the flexibility to offer competitive compensation and promote the recruitment and motivation of competent leaders.

The activities of these committees are operational and the various committees established by the Board may cover these issues, whenever necessary.

The company does not have this expertise, which falls within the realm of the scientific community.

TABLE 49

## TYPES OF SHAREHOLDER PROPOSALS GENERALLY SUPPORTED BY THE CAISSE

Proposals	"FOR" Votes	"FOR" Vote Reasons	Company Examples	"AGAINST" Vote Reasons
Annual election of directors	10 out of 10 proposals (100%)	The annual election leads to the periodic evaluation of director effectiveness and contributions.	Abercrombie & Fitch Co. Danaher Corporation Massey Energy Company	N/A
Separation of Board Chairman and CEO positions	20 out of 36 proposals (56%)	The Board did not appoint an independent director to act as lead director and ensure effective work progress.	The Boeing Company The Coca-Cola Company Wells Fargo & Company	The Board appointed an independent director to act as lead director and ensure effective work progress.
Adoption and disclosure of a succession planning policy for the President and Chief Executive Officer	5 out of 5 proposals (100%)	Succession planning is one of the Board's major responsibilities. It should adopt a succession plan establishing the skills for the positions. The main elements of this plan should be disclosed to shareholders.	Bank of America Corporation Fedex Corporation Verizon Communications Inc.	N/A
Retaining a significant portion of shares under incentive compensation plans	27 out of 29 proposals (93%)	Long-term share holdings align the interests of officers and shareholders.	American Express Company Citigroup Inc. The Goldman Sachs Group, Inc.	Company compensation programs provide procedures for share holdings, adequately aligning the interests of officers and shareholders.
Performance-linked compensation	3 out of 6 proposals (50%)	Establishing performance goals promotes the link between executive compensation, company performance and shareholder gains.	Comerica Incorporated Coventry Health Care, Inc. Pulte Homes, Inc.	Existing compensation programs promoting the link between compensation and performance or certain aspects of the proposal are too restrictive.
Elimination of the qualified majority vote (66.67% or more shares outstanding)	23 out of 23 proposals (100%)	The vote by an absolute majority (more than 50% of the outstanding shares) is sufficient to approve company acts in the ordinary course of business.	Alcoa Inc. Baxter International Inc. Kellogg Company	N/A
Adoption of greenhouse gas (GHG) emission reduction targets and publication of a report on the action plan	5 out of 5 proposals (100%)	The company should take the necessary steps to comply and protect the environment in which it operates. Furthermore, the disclosure of GHG emission information permits shareholders to better assess the risks.	CMS Energy Corporation Exxon Mobil Corporation Lennar Corporation	N/A
Publication of a sustainable development report	9 out of 9 proposals (100%)	The proposal promotes the use of a framework for reporting the economic, environmental and social aspects of the company's activities.	C.R. Bard, Inc. Google Inc. Suntrust Banks, Inc.	N/A

## Responsible Investment Report

### Shareholder engagement through direct dialogue with companies

Direct dialogue between the Caisse and its portfolio companies is done in many ways and focuses on environmental, social and governance (ESG) issues.

The Caisse establishes this dialogue upon exercising its voting rights, with the aim of obtaining more information or making its voting position known to companies. At the same time, the Caisse conveys specific issues to companies and, in turn, holds discussions on them, either in person or via conference call.

With this approach, the Caisse hopes that its portfolio companies:

- conduct their activities in compliance with the rights and freedoms guaranteed under the law and prohibit discrimination.
- respect the rights of workers, take the necessary steps to provide them with a safe and healthy environment and prohibit all forms of abuse.
- take measures to respect and protect the environment in which they operate.
- respect the communities in which they operate and promote their development.

### Shareholder engagement through collaborative initiatives

The Caisse collaborates with many investor groups involved in responsible investment matters.

In 2010, the Caisse participated in an initiative launched by a group of 18 signatories putting forward a series of Principles for Responsible Investment (PRI) – which called for 21 targeted companies to disclose how they fight corruption. Letters were sent to these organizations and ten out of the 21 responded by disclosing elements related to existing practices and policies for preventing and controlling corruption.

## EXAMPLES OF DIALOGUE WITH COMPANIES

### Compensation program amendments

The Caisse does not support a plan that gives discretion to the Board when it comes to the amendment of certain terms, such as the exercise price and expiration of options. These should be issued at a minimum of 100% of the fair market value and their expiration should not exceed 10 years for all plan participants. The Caisse contacted the company to express its position. The company subsequently followed the correct amendment procedure in accordance with best governance practices. The company issued a press release confirming its commitment.

### Director independence

The Caisse opposed the election of a director because he was not independent of management and served on the Nominating Committee. There was discussion with the company, which has taken note of the Caisse's position for the future.

### Impact of activities on local communities

In recent years, the Caisse has established regular dialogue with an oil company that operates in an area of political conflict. Respect for human rights and the impact of logging on communities are the main topics of discussion. A site visit was made to ensure the implementation of programs and security measures. The company has demonstrated that it provides support and resources to its employees and the public to deal with this situation.

### Environmental risks

The Caisse has held numerous discussions with a mining company about major environmental issues at a site with difficult geological conditions. The company is committed to taking steps to improve the management of these environmental problems and reduce their negative impact. It developed a particular method of using waste from its operation and implemented an environmental indicator monitoring system for this mine that it plans to adopt at all its sites. The Caisse has regularly monitored the implementation of these measures.

### **Shareholder engagement through dialogue with stakeholders**

During 2010, many discussions were held with stakeholders, including NGOs, a mining association and shareholder groups. These discussions led to a better understanding of their concerns about certain social and environmental issues related to the operations of some companies.

Through investor groups, the Caisse mostly collaborates in representations made with regulatory authorities. Furthermore, when making company visits, the Caisse holds discussions, whenever possible, with local NGOs. Finally, the Caisse builds relationships with universities for responsible investment-related matters.

### **EXAMPLE OF DIALOGUE WITH A MINING INDUSTRY STAKEHOLDER**

The Caisse has a representative on the Mining Association of Canada's Community of Interest Panel. This association developed the Towards Sustainable Mining (TSM) initiative to improve the mining industry's performance by aligning its actions with the priorities and values of Canadians.

## **2. ESG CRITERIA INTEGRATION**

The integration of ESG factors in the Caisse's risk analysis activities is entrenched in its Equity Markets group. Over time, many tools have been developed to enable managers to incorporate ESG criteria in their investment analysis. The institution's managers closely monitor these factors for any impact on their portfolios.

The integration model developed by the Caisse's managers is based on an exhaustive list of items to verify with a company. This includes the composition of the Board, company management, environmental protection measures and existing local community acceptance policies, among others. The managers conduct a qualitative assessment of the information from a risk and economic value impact standpoint for shareholders. A score derived from this exercise is assigned and integrated into more comprehensive company analysis.

Research is also an important part of integrating ESG criteria. The Caisse encourages ESG research, primarily by requiring securities dealers to produce reports with an analysis on these factors, as well as by subscribing to specialized research firms services and participating in conferences on the subject.

## **3. EXCLUSION: SPECIAL CASES**

The portfolio exclusion of securities is an exceptional measure that can be taken by the Caisse based on certain circumstances. For example, these circumstances may result from a company being in breach of an international convention.

In 2010, the Caisse excluded from its portfolio companies that manufacture weapons banned by the Ottawa Convention on Landmines and the Oslo Convention on Cluster Munitions. These securities, however, could be reinstated if the companies in question ceased to manufacture such weapons.

## **4. RESPONSIBLE INVESTMENT COMMITTEE**

The newly created Responsible Investment Committee will ensure the consistency of the Caisse's responsible investment approach, which takes into account depositors' expectations in this respect.

## **CONCLUSION**

In 2010, the Caisse revamped its approach and its Policy on Responsible Investment. This exercise led to the adoption of a new version of the policy to ensure its closer alignment with the Caisse's recent activities. The Caisse recognizes the importance of responsible investment in the pursuit of sustainable economic development. Accordingly, it aims to continue its activities in this area while taking into account the risks and size of its portfolio investments.



# Reports of Board of Directors and Board Committees

# Board of Directors' Report

## HIGHLIGHTS

**01** Implementation of several initiatives to simplify the Caisse's structure and refocus on its core activities.

**02** Strategic discussions on future challenges and investment opportunities.

**03** Review of the Operations and Information Technology group's business model and organizational structure.

## BOARD OF DIRECTORS

### MANDATE

The Board of Directors:

- Ensures that the Caisse is managed in compliance with the provisions of its constituting statute and bylaws.
- Ensures that the institution takes the necessary steps to achieve the objectives stated in its mission.
- Enacts bylaws and approves the Caisse's main guidelines and policies with respect to investment operations, responsible investment, risk management oversight and delegation of authority.
- Receives all matters that call for special attention due to their intrinsic importance or to their impact on either the Caisse's portfolio or its asset allocation.
- Reviews and approves the Caisse's strategic plan.
- Reviews and approves the Caisse's annual business plan, and monitors management's evaluations of the economic and financial environment throughout the year.
- Examines and approves the Caisse's budgets, financial statements and Annual Report.
- Assesses the integrity of internal controls, information disclosure controls and information systems.
- Approves the financial disclosure policy.
- Approves human resources policies, compensation standards, compensation scales and other employment conditions for Caisse officers and employees.
- Determines the compensation standards, compensation scales and other employment conditions for the President and Chief Executive Officer, according to the parameters set by the Government in consultation with the Board.
- Appoints the members of senior management on recommendation by the President and Chief Executive Officer.
- Develops and oversees implementation of the Caisse's rules, procedures and policies on governance in collaboration with the Governance and Ethics Committee.
- Approves the rules of ethics and professional conduct that apply to Caisse Board members and to officers and employees of the Caisse and its subsidiaries.

As required by law, the Board of Directors has formed an Audit Committee, a Human Resources Committee, a Governance and Ethics Committee, and a Risk Management Committee.

### COMPOSITION

As at December 31, 2010, the Board consisted of 14 members out of a maximum of 15.

The Board consists of its Chairman, the President and Chief Executive Officer, depositors' representatives and independent members. The Act respecting the Caisse stipulates that at least two-thirds of the directors, including the Chairman, must be independent.

In 2010, after consulting the Board, the Québec government reappointed Ouma Sananikone as an independent director for a four-year term.

Table 50 provides information regarding member attendance at Board and committee meetings during fiscal 2010.

### REMUNERATION OF INDEPENDENT DIRECTORS

The remuneration of the Caisse's independent directors is determined by Order-in-Council of the Québec government. Under this decree, the following compensation was paid to independent directors, with the exception of the Chairman (see Table 51).

Directors are also entitled to the reimbursement of their travel and living expenses, where applicable.

### REMUNERATION OF THE CHAIRMAN OF THE BOARD

Annual remuneration of the Chairman of the Board is fixed at \$195,000 by the Québec government. In addition, the Chairman is entitled to the reimbursement of hospitality expenses incurred in the performance of his duties – up to \$15,000 per year.

TABLE 50

DIRECTOR ATTENDANCE AT BOARD AND COMMITTEE MEETINGS FOR 2010<sup>1</sup>

Member	Board of Directors		Audit Committee		Risk Management Committee		Human Resources Committee	Governance and Ethics Committee	
	8 reg.	6 spec.	7 reg.	1 spec.	8 reg.	2 spec.	8 reg.	8 reg.	2 spec.
Elisabetta Bigsby	8	5	—	—	—	—	8	—	—
Claudette Carbonneau	8	5	—	—	—	—	—	7	1
Louise Charette	8	6	7	1	—	—	—	8	2
Jocelyne Dagenais	6	6	—	—	2/3	—	—	—	—
Michèle Desjardins	8	5	—	—	—	—	—	8	2
Pierre Fitzgibbon	7	6	7	1	8	1/1	—	—	—
A. Michel Lavigne	8	6	7	1	8	2	—	—	—
Jean Pierre Ouellet	8	6	—	—	—	—	8	6/6 <sup>2</sup>	2
Réal Raymond	8	5	—	—	8	2	—	—	—
François R. Roy	8	6	7	1	8	2	—	—	—
Michael Sabia	8	6	—	—	—	—	—	—	—
Ouma Sananikone	7	6	—	—	8	2	8	—	—
Robert Tessier	8	6	—	—	—	—	8	2/2	—
André Trudeau	6	5	—	—	—	—	—	—	—

1. Directors justify their absences from regular meetings of a Committee or the Board to the Caisse's Secretariat. During 2010, directors were not able to attend certain meetings due mainly to identified conflicts of interest, changes to the regular meeting schedule requested by the Caisse and family or work commitments.

2. During the year, Mr. Ouellet ceased to be Chairman and a member of this Committee.

TABLE 51

## COMPENSATION PAID IN 2010 TO ORDER-IN-COUNCIL INDEPENDENT DIRECTORS

Director	Annual compensation (\$17,042.75) <sup>1</sup>	Compensation as Committee Chair (\$5,326.25) <sup>1</sup>	Attendance fees (\$800) <sup>1,2</sup>	Total compensation
Elisabetta Bigsby	\$17,042.75	\$5,326.25	\$15,570.00	\$37,939.00
Claudette Carbonneau <sup>3</sup>	\$17,042.75	—	\$15,170.00	\$32,212.75
Louise Charette	\$17,042.75	—	\$24,754.00	\$41,796.75
Michèle Desjardins	\$17,507.93 <sup>4</sup>	—	\$15,974.00	\$33,481.93
Pierre Fitzgibbon <sup>5</sup>	\$17,042.75	—	\$24,346.00	\$41,388.75
A. Michel Lavigne <sup>5</sup>	\$17,042.75	\$5,326.25	\$26,746.00	\$49,115.00
Jean Pierre Ouellet <sup>5</sup>	\$17,042.75	\$4,436.97	\$23,550.00	\$45,029.72
Réal Raymond <sup>5</sup>	\$17,042.75	\$5,326.25	\$19,158.00	\$41,527.00
François R. Roy	\$17,507.93 <sup>4</sup>	—	\$24,754.00	\$42,261.93
Ouma Sananikone	\$17,042.75	—	\$23,158.00	\$40,200.75
<b>Total</b>				<b>\$404,953.58</b>

1. In accordance with the terms of the current Order-in-Council, a 0.5% increase was applied on April 1, 2010.

2. The attendance fee for each special or short Board or Committee meeting held by conference call is \$400.

3. This director did not receive her compensation directly, as per her instructions to the Caisse.

4. These directors were appointed at the end of 2009. An adjustment of \$465.18 was paid in 2010 as compensation for 2009.

5. These directors received attendance fees for meetings of the Special Financing Committee created under the financing program.

## Board of Directors' Report

### ACTIVITY REPORT

#### **Compliance with the Act respecting the Caisse**

Throughout the year, the Board ensured that the Caisse's activities complied with the Act and relevant regulations.

#### **Strategic planning**

The most recent strategic planning exercise was split into two chapters. Phase 1 consists of five strategic priorities approved by the Board in 2009 – whose implementation was completed or initiated in 2010.

Accordingly, 2010 represented a transition period that led to a major reorganization. The objective was to reposition the Caisse on many levels, namely by simplifying its structure and refocusing on its core activities in a fiduciary spirit to ensure it can fulfill its mission and provide the long-term returns expected by its depositors.

#### **Establish a new collaboration model with depositors**

The Board ensured that the Caisse reviews its depositor relationships to gain a greater understanding of their return and risk expectations and better report on its investment activities. This exercise has, for instance, led to the review of depositors' service agreements and accountability reports.

#### **Provide long-term, risk-adjusted, liability-driven returns**

The Board authorized the revamp of the specialized portfolios to offer depositors portfolios better aligned to their needs. The Board, with the assistance of the Risk Management Committee, consequently approved amendments to the investment policies of the specialized portfolios, value added objectives of actively managed specialized portfolios and benchmark indexes for certain portfolios.

#### **Leadership in Québec**

The Board supported senior management's proposed strategies and organizational structure to ensure that the Caisse strengthens its leadership in Québec. This strategy has, for example, led to partnerships that support the growth projects of Québec companies and partnerships with Québec universities in connection with various financial research programs. For more information, see the section on the Caisse's contribution to Québec economic development on page 65.

#### **Strengthen risk management in an environment of considerable uncertainty**

In 2010, the Caisse continued to refine its risk management practices. The Board therefore ensured, with the assistance of the Risk Management Committee, the implementation of a comprehensive approach to risk management, involving the enhanced collaboration of various investment groups, risk officers and senior management. For example, the Board approved an underweight strategy in its Equity portfolios due to increased market risk, particularly related to the European crisis. The Board also authorized the review of many risk management measures, including certain additions to the integrated risk management policy and the monitoring of a new credit risk measurement methodology implementation. In addition, it tracked major investments with a significant impact on portfolio risk levels and concentrations. For more details on the activities of the Board and Risk Management Committee, see the Report of the Risk Management Committee on page 116.

#### **Create a service culture that inspires collaboration, rigour and achievement**

To achieve its objectives, the Caisse must ensure the commitment of its employees and develop a client-centric culture. In 2010, the Board, in collaboration with the Human Resources Committee, supported senior management in simplifying and aligning compensation programs with the Caisse's strategic priorities. The Board also supported senior management in implementing an integrated talent management strategy, including the completion of a succession planning exercise for key positions and the establishment of professional development plans. See the Report of the Human Resources Committee on page 103 for more details on the human resource management activities of this committee and the Board.

#### **Business plan**

Each Caisse business group presented its annual business plan to the Board. The Board adopted the Caisse's business plan and annual budget. It also regularly received senior management reports on changes in the Caisse's business.

The Board was able to effectively oversee the Caisse's activities and the development of strategic priorities, contributing constructively to the process.

**Financial results, internal controls and management systems**

With the assistance of the Audit Committee, the Board fulfilled its responsibilities with respect to financial results and internal controls, mostly by reviewing the quarterly financial statements, approving the annual combined financial statements, evaluating the integrity of the controls applied to various data for the financial statements and related notes and monitoring the internal audits. See the Report of the Audit Committee on page 98 for more information on the responsibilities of this committee and the Board.

Moreover, the Board received reports analyzing the returns of the Caisse's various investment groups. It also approved the press release announcing the Caisse's financial results, as well as its Annual Report.

**External financing program**

In 2009, the Board approved the launch of an external financing program to replace a portion of short-term debt with longer-term debt. A U.S. market bond issue was completed at the end of 2009. In 2010, the Board approved the required documentation for bond issues in the Canadian and the European markets. These two issues completed the Caisse's external financing program, as approved in 2009.

**Repositioning of the Operations and Information Technology group**

After grouping the Operations and Information Technology (IT) teams, two comprehensive reorganizations were carried out: one in fall 2009 within the Operations group and another in 2010 within the Information Technology group. Both reorganizations were aimed at optimizing the use of the Caisse's operational and information resources.

The Board, in collaboration with senior management, extensively reviewed the IT group's new business model and organizational structure. The repositioning is aimed mostly at improving the overall delivery of IT services, increasing agility, flexibility and speed, strengthening links with managers, better controlling operations and reducing costs.

**Senior management supervision**

The Board, assisted by the Human Resources Committee, adopted the detailed objectives of the President and Chief executive Officer for 2010. The Board also reviewed the performance of the President and Chief Executive Officer based on the objectives set at the beginning of the year and concluded that his contribution had largely exceeded these targets.

The Board examined the President's evaluation of senior officer performance. During its meetings, it also regularly received executive presentations on their business activities. On the Human Resources Committee's recommendation, the Board approved the 2010 employee conditions and 2009 senior management bonus level. It also approved the appointment and compensation of new Executive Committee members.

**Corporate governance**

For the Board, 2010 provided the opportunity to strengthen the cohesion of its members and consolidate the establishment of a sound governance culture. The Board, assisted by the Governance and Ethics Committee, maintained the highest governance standards. It held discussion sessions with the President and Chief Executive Officer without the presence of other senior management members and in camera discussion sessions. Also, through the Governance and Ethics Committee, it reviewed the Director Code of Ethics and Professional Conduct, examined statements of interest submitted by each director and monitored the directive on the review of transactions in securities of companies with ties to a Caisse director.

After receiving Jean Pierre Ouellet's resignation as a member and Chairman of the Governance and Ethics Committee, the Board appointed Robert Tessier to assume these roles.

The Board's relationship with senior management, aimed at being constructive and based on trust and respect of each other's roles, was also enhanced through presentations by investment group heads at Board meetings throughout 2010, as well as senior management presentations at meetings held the day before the Board convened.

For more information on the governance efforts of the Board and this committee, see the Report of the Governance and Ethics Committee on page 101.

# Report of the Audit Committee

## HIGHLIGHTS

**01** Implemented a joint audit process for the Caisse's books and accounts.

**02** Reviewed the financial statement preparation process, particularly the investment valuation methodology.

## THE AUDIT COMMITTEE

### MANDATE

The Audit Committee:

- Oversees the compliance of the financial statements with the Caisse's financial position.
- Examines the financial statements with the auditors and recommends their approval to the Board of Directors.
- Ensures that adequate and effective internal control mechanisms are in place.
- Ensures that a risk management process for the Caisse's operations is in place.
- Ensures that a plan for an optimal use of resources is in place and monitors its progress.
- Reviews any activity that could adversely affect the Caisse's sound financial position and informs the Board of Directors in writing of any management operation or practice that is unsound or does not comply with the laws, regulations or policies governing the Caisse.
- Recommends to the Board the appointment of the Vice-President, Internal Audit and approves the audit plan.
- Receives reports from the Vice-President, Internal Audit on matters such as the execution of internal control mechanisms, the risk management process, as well as the implementation of a plan for the optimal use of resources.
- Ensures that the organizational structure provides the Internal Audit team with the independence required to perform its role effectively.

During the year, the Committee reviewed its mandate and that of its Chair, in conjunction with the Governance and Ethics Committee.

### COMPOSITION (as at December 31, 2010)

Four independent members, including professionals with accounting or finance expertise, possessing the experience and knowledge to read and understand the financial statements and properly fulfill their role. The Chairman of the Board regularly attends Committee meetings.

- Chair: A. Michel Lavigne (guest member at the Risk Management Committee meetings)
- Members: Louise Charette, Pierre Fitzgibbon and François R. Roy

### REPORT

Number of regular meetings in 2010: 7

After each meeting, the Committee provided a verbal and written report on its activities to the Board of Directors. Committee members also met regularly without the presence of senior management.

The report below, which describes the issues discussed and decisions taken during the year, was approved by the Committee members.

### Joint audit

In November 2009, the Québec government adopted a decree designating Ernst & Young to audit the Caisse's books and accounts, as part of a joint audit with the Auditor General of Québec, for the years ending December 31, 2010 to 2014.

In order to optimize this first year of joint audit, both for the auditors and senior management, Ernst & Young carried out a shadowing for the audit of the financial statement books and accounts as at December 31, 2009. This engagement allowed the firm to present its perspective to senior management and the Audit Committee without acting as a signatory to the December 31, 2009 auditor report. The shadowing also helped the Audit Committee adjust to the dynamics of a joint audit. With respect to this new auditor, the Committee carried out the following activities:

- Reviewed the monitoring report on the shadowing, particularly regarding the opening balances at January 1, 2010 and the implications of the joint audit on the 2009 audit and 2010 joint audit exercises.
- Recommended to the Board the adoption of an external auditor independence policy and reviewed the monitoring reports regarding compliance with this policy.

### Financial information

The Committee fulfilled its financial information responsibilities as follows:

- Reviewed the 2009 Combined Financial Statements with the Auditor General of Québec, in the presence of the co-auditor, and the following items:
  - The financial statement preparation process.
  - The valuation of over-the-counter liquid investments, illiquid investments and ABTNs.
  - The methodology and parameters for measuring the fair value of ABTN investments.
  - The validation of the notional amount of derivatives instruments by an external firm.
  - The external audit of returns to ensure their calculation and presentation complies with industry standards.
- Reviewed the report on the financial certification process that enables the President and Chief Executive Officer and Acting Chief Financial Officer to certify publicly that the disclosure controls and procedures are adequate and effective, and that the internal financial reporting controls are adequate.
- Reviewed the activity reports of each Caisse real estate subsidiary's Audit Committee.
- Verified that an independent valuation of the fair value of over-the-counter liquid investments, private equity investments, ABTNs and the Caisse's real estate assets has been carried out semi-annually, including:
  - The independent review of valuation data for 10 private equity investment files and the valuation of the fair market value of five other private equity investment files – by a renowned firm.
  - The independent external valuation of the fair value of certain liquid securities, real estate debt securities and corporate debt portfolio securities – by two world-renowned experts.
- Examined a benchmarking report on the fair market value determination processes and methods for private equity and infrastructure investments.
- Recommended to the Board, for approval, amendments to the private equity and infrastructure investment valuation policy.
- Recommended the adoption of the Combined Financial Statements to the Board.
- Received the report of the Auditor General of Québec issued to the Caisse's senior management after its audit for 2009.
- Recommended that the Board approve an updated information disclosure policy.
- Reviewed the press releases pertaining to the Caisse's financial results.
- Reviewed quarterly financial statements, operating expense budget monitoring and year-end budget estimates.
- Discussed with the co-auditors their audit plan for the Caisse's 2010 financial statements.
- Reviewed the work on the new specialized portfolio offering's implementation.
- Reviewed and monitored the decisions of Canadian and international authorities on the application of international financial reporting standards, and monitored the preparatory work for implementing these standards.
- Held regular discussions with Finance personnel without the presence of senior management.
- Held regular meetings with the co-auditors without the presence of senior management members to discuss various aspects of their mandate.

## Report of the Audit Committee

### Internal audit

Reporting to the Audit Committee, Internal Audit is an activity that helps the Caisse achieve its objectives by adopting a systematic and methodical approach to evaluating risk management, control and corporate governance processes, and making proposals to enhance their effectiveness. Accordingly, during 2010, the Committee carried out the following activities with the Vice-President, Internal Audit:

- Reviewed the 2010-2011 internal audit strategic plan and 2010 business plan of the Vice-President, Internal Audit.
- Reviewed and adopted the 2010 internal audit plan.
- Reviewed progress reports from the Internal Audit division, under the internal audit plan, mostly on internal control mechanisms, risk management process components and the optimal use of resources.
- Examined the report on the creation of oversight roles to enable the board and its committees to fulfill their responsibilities.
- Reviewed the monitoring reports on the framework between the Caisse's Vice-President, Internal Audit and the internal audit teams of the real estate subsidiaries.
- Reviewed the activity report of the Internal Audit division for 2009.
- Monitored the implementation of the Internal Audit division's recommendations by the Caisse's senior management.
- Evaluated the performance of the Vice-President, Internal Audit, and made a recommendation about her compensation to the Board.
- Ensured that the Internal Audit team can act independently from the Caisse's senior management.
- Held periodic discussions with the Vice-President, Internal Audit without the presence of senior management.

### Internal controls and plan for the optimal use of resources

The Committee reviewed many aspects of internal controls and the optimal use of resources during 2010. To this end, it carried out the following activities, among others:

- Discussed senior management's overall self-assessment of the general control environment's effectiveness.
- Reviewed the Internal Audit assessment report on general environment and information technology processes and controls.
- Examined the report on the Caisse's Information Technology group issues and priorities.
- Reviewed the quarterly reports on compliance with investment limits as specified in the Act governing the Caisse.
- Monitored the investments made under the last paragraph in Section 37.1 of the Act governing the Caisse.
- Reviewed the delegation of authority and recommended certain changes to the Board for approval.
- Monitored activities surrounding the implementation of a plan for the optimal use of resources.

### Risk management

The Board of Directors established the Risk Management Committee to support the Audit Committee in exercising its responsibility to implement a risk management process. The Committee therefore carried out the following activities to monitor all risk management efforts:

- Received copies of the minutes of the Risk Management Committee meetings and the annual report on integrated risk management.
- Received a copy of the certificates of compliance with depositors' investment policies and the investment policies of the Caisse's specialized portfolios.
- The Chair of the Committee attended Risk Management Committee meetings.
- Received reports on each Risk Management Committee meeting, tabled by its Chair, during Board meetings.

### USE OF EXTERNAL EXPERTS

The Audit Committee did not use any external expert services in 2010. However, it supported senior management when it used external firms for an independent review of private equity, liquid security, real estate debt and ABTN valuation data.

# Report of the Governance and Ethics Committee

## HIGHLIGHTS

**01** The Committee reviewed the method for preparing and transmitting information to directors to ensure that sufficient and relevant information is received promptly.

**02** The Committee reviewed the Responsible Investment Policy.

## THE GOVERNANCE AND ETHICS COMMITTEE

### MANDATE

The Governance and Ethics Committee:

- Assists the Board in establishing and implementing principles and practices that foster a sound governance culture at the Caisse.
- Establishes the rules, structures and procedures that enable the Board to act independently of management.
- Offers orientation and continuing education programs for directors.
- Advises the Board on the composition and mandates of both regular and special committees aimed at helping the Caisse run its operations more smoothly.
- Recommends an approach to evaluating both the directors and Board.
- Establishes, in collaboration with the Human Resources Committee, the skill and experience profiles for selecting independent directors, and submits them to the Board.
- Reviews and recommends to the Board ethics, professional conduct, responsible investment and governance rules, codes or policies that must be promoted when exercising voting rights with respect to portfolio companies.

The Committee reviewed its mandate and that of its Chair during 2010.

### COMPOSITION (as at December 31, 2010)

Four independent members.

- Chair: Robert Tessier
- Members: Claudette Carbonneau, Louise Charette and Michèle Desjardins

## REPORT

Number of regular meetings in 2010: 8

After each meeting, the Committee provided the Board with a verbal and written report on its activities.

The following report, which was approved by the Committee members, describes issues that were the subject of discussion or decisions during the year.

### Governance rules

Following efforts to strengthen board governance in 2009, the Committee ensured high-level adherence to governance practices in 2010. To this end, it carried out the following work.

### The Board and its committees

- Reviewed the responsibilities outlined in the mandates of the Board, its committees and their chairs.
- Reviewed the responsibilities delegated to the President and Chief Executive Officer, as outlined in his mandate.
- Ensured that key individuals in the Caisse's management or externally are available to explain various items on the agenda of Board meetings, and that there is enough time for a full discussion.
- Ensured that the Board has all the information and time it needs to analyze any challenges faced by the Caisse.
- Reviewed the process for preparing and transmitting information to Board members and committees to ensure they receive sufficient and relevant information promptly.
- Verified throughout the year that discussion sessions were held without members of management and ensured that there was adequate time for full discussion by the directors.
- Discussed and recommended a director continuing education program to the Board and provided presentations at Board meetings as well as outside this formal framework, in order to allow directors to discuss issues related to the performance of their role.

## Report of the Governance and Ethics Committee

### Caisse

- Reviewed the governance structures of the Caisse's subsidiaries and investments to ensure that they allow the Board to fully assume its responsibilities.
- Discussed the applications for Director of the Caisse's real estate subsidiaries.
- Analyzed and discussed the process for appointing directors to the Board of portfolio companies.
- Recommended to the Board, for approval, amendments to the Policy on Contracts for the Acquisition or Leasing of Goods and Services.
- Reviewed the Equity Markets group's commission management process.
- Recommended to the Board, pursuant to the terms of the donation and sponsorship policy, the approval of a partnership between the Caisse and a Québec-based financial organization.

### Code of Ethics and Professional Conduct

The committee annually reviews the Code of Ethics and Professional Conduct in effect. To this end, it carried out the following activities:

- Reviewed the Director Code of Ethics and Professional Conduct, interpreting code provisions, as required for its application and presentation of a report to the Board.
- Received the report on the implementation of the Caisse Officer and Employee Code of Ethics and Professional Conduct. Moreover, the Committee revised this Code in early 2011.
- Examined, on behalf of the Board, declarations of interest submitted by the directors in accordance with the provisions in effect and transmitted these statements to the authorities designated by the Act respecting the Caisse.
- Monitored the directive on the review of transactions in securities of companies with ties to a Caisse director.

### Composition of the Board and Committees

The Committee reviews the composition of the committees and Board annually to ensure that members have the experience and skills to contribute fully to the work of these bodies. To this end, the Committee:

- Reviewed, in collaboration with the Human Resources Committee, the skills and experience profiles of independent directors.
- The Chair reviewed the Board's composition, each director's term of office and the Board's skills and expertise as a whole.
- Recommended the composition and chairmanship of the committees to the Board.

### Committee and Board operation

- Reviewed the process for evaluating the performance of the Board, its Chair and its committees, including self-evaluation by the directors.
- Analyzed the Board and committee evaluation results and recommended improvements to certain processes, as required.

### Responsible Investment Policy

The Caisse adopted a Responsible Investment Policy. In this respect, the Committee carried out the following activities:

- Discussed the implementation of the Responsible Investment Policy in 2009 and 2010.
- Recommended to the Board, for approval, amendments to the Responsible Investment Policy.
- Examined the report on the Caisse's exercise of voting rights with respect to portfolio companies, and discussed principles governing this exercise.
- Reviewed the Real Estate group's business practices in emerging market countries.

### USE OF EXTERNAL EXPERTS

The Governance and Ethics Committee did not use the services of an external expert in 2010.

# Report of the Human Resources Committee

## HIGHLIGHTS

- 01** Adopted a senior management succession plan. **02** Implemented a new compensation policy.

## HUMAN RESOURCES COMMITTEE

### MANDATE

The Human Resources Committee reviews the strategic direction of integrated talent management. It submits human resources policies to the Board for approval and ensures their implementation. The Committee pays special attention to the compensation policy, for which it receives the Caisse's annual reference market data. In addition, it reviews and submits the Caisse's employees compensation and other employment conditions to the Board for approval.

The Committee develops the expertise and experience profile for the President and Chief Executive Officer (CEO) appointment. It examines the annual objectives of the President and CEO, evaluating his performance and recommending his compensation and other employment conditions to the Board for approval, taking into account the parameters established by the Government.

The Committee reviews the recommendations of the President and CEO on the appointment, objectives, performance evaluation and compensation of the Caisse's senior executives. It examines the responsibilities of senior executives and ensures the existence of succession planning mechanisms.

In collaboration with the Governance and Ethics Committee, the Human Resources Committee develops the expertise and experience profile for the appointment of independent directors and submits them to the Board for approval.

During 2010, the Committee, together with the Governance and Ethics Committee, also reviewed its mandate and that of its Chairman.

### COMPOSITION (as at December 31, 2010)

The Committee is composed of four independent members:

- Chair: Elisabetta Bigsby
- Members: Jean Pierre Ouellet, Ouma Sananikone and Robert Tessier

### ACTIVITY REPORT

The Committee met eight times in 2010. During the year, it paid special attention to integrated talent management, focusing particularly on:

- Succession planning
- Talent management
- The incentive compensation policy

After each meeting, the Committee provides a verbal and written report on its activities to the Board. In addition, Committee members met regularly without the presence of senior management. This report, approved by Committee members, highlights their work.

### Senior management

The Committee considered and recommended to the Board of Directors the approval of Mr. Sabia's objectives as President and CEO for fiscal year 2010. It also examined Mr. Sabia's proposals for appointments to the Caisse's Executive Committee.

## Report of the Human Resources Committee

In addition, the Committee, in particular, reviewed and recommended the following to the Board for approval:

- Hiring or promoting employees at the Senior Vice-President level or higher and the employment conditions to ensure their compliance with compensation policy.
- Evaluating performance and determining the total compensation (base salary, incentive compensation, pensions and benefits) for senior executives for 2009 and 2010.
- Total compensation conditions for the President and CEO for 2011.
- Succession plan for senior management positions and the President and CEO.

### Integrated talent management strategies and key policies

The Committee discussed several integrated talent management strategies and key policies during the year 2010 to provide the Caisse with truly integrated talent management. To this end, the Committee, in particular, carried out the following activities:

- Established certain organizational development priorities.
- Analyzed the management of dashboards and operational risk management strategies related to human resources management.
- Reviewed the strategy of professional and leadership development plans for the Caisse's employees.
- Recommended to the Board, for approval, a career progression model for senior professional positions.
- Recommended to the Board, for approval, a collegial process for creating new positions and awarding promotions.
- Reviewed the performance management strategy and, more particularly, the quality of the goal setting and continuous feedback process.

### Independent Board of Directors

The Committee proceeded to review the expertise and experience profile of independent Board of Directors in collaboration with the Governance and Ethics Committee.

### Use of external experts

The Board of Directors and its committees may, in exercising their functions, use external experts. In establishing the new incentive compensation program and monitoring its implementation, the Committee and the Board used the services of Hugessen Consulting, an independent consulting firm recognized for its expertise in the compensation of pension fund personnel.

## COMPENSATION POLICY

### Committee's incentive compensation efforts

The Committee continued the work it had undertaken in 2009 to develop and implement a new compensation policy. With the assistance of its external advisor, Hugessen Consulting, it analyzed the various compensation policy elements, particularly those related to incentive compensation, and made recommendations to the Board for approval. This program is described in the Report on Compensation Policy section of the 2009 Annual Report on pages 86 to 91.

Accordingly, the Committee, in particular, analyzed and recommended the following to the Board for approval:

- Potential incentives for positions at all levels.
- Components of incentive compensation and their relative weight in its calculation.
- Incentive compensation clawback.
- Deferred and co-invested mechanism for the incentive compensation program (for more details, see page 108).

Moreover, in accordance with the transitional incentive compensation program adopted for this period, the Committee reviewed the incentive compensation for 2009. It also discussed the incentive compensation and salary conditions of the Caisse's employees for 2010, recommending them to the Board for approval.

Finally, the Committee received from its external advisor, Hugessen Consulting, an update on compensation market trends to ensure proper implementation of its compensation policy and independent advice on the application of the new incentive compensation program in 2010.

### Regulation Respecting Internal Management

The Caisse's compensation policy is governed by Appendix A of the Regulation Respecting Internal Management, revised by government decree in 1996. This policy:

- Defines the maximum levels for total employee compensation and reference markets.
- Indicates that the data reflecting the reference market profile must be compiled through an annual survey by a recognized independent firm, and must be administered and analyzed according to generally accepted methodologies and rules in this field.
- Stipulates that the Caisse's payroll must not exceed 100% of the salary range midpoint.

In 2010, the Caisse retained the services of Towers Watson for benchmarking the markets. The company selection criteria for the reference markets include the following: size, industry, companies that recruit talent similar to the profiles the Caisse seeks, organizations offering products and innovative and diverse investments, firms recognized for their best practices in human resources, companies with performance-driven cultures and businesses participating in the Towers Watson database.

#### **Reference markets and compensation level position<sup>1</sup>**

For the President and CEO position, the reference market includes a sample of eight large Canadian pension funds, whose list is shown in Table 57. For this position, total compensation must be between the median and third quartile (75<sup>th</sup> percentile) of the reference market, depending on whether the Caisse's performance is average or superior.

For investment duties, the Canadian institutional investment market serves as the reference. This must include a representative sample, including institutions, insurance companies, trust companies, pension funds, investment advisors, brokerage firms and fund managers or their counterparts in similar industries. The current sample includes 60 organizations. The list can be found in Table 55. For these positions, the total compensation must be below the top 10 percent (90<sup>th</sup> percentile) of the reference market.

For non-investment duties, the Québec market serves as the reference, which must include public sector jobs. It therefore contains a representative sample of large public and private-sector Québec firms and private financial companies. The current sample includes 49 organizations. The list is shown in Table 56. For these positions, the total compensation must be at the third quartile (75<sup>th</sup> percentile) of the reference market.

#### **Strategic objectives of the compensation policy**

The Caisse must rely on highly skilled employees who enable the institution to achieve its mission: achieve an optimal return on depositors' capital in accordance with their investment policies, while contributing to Québec's economic development. Therefore, the total compensation policy pursues the following three objectives:

**1. Pay for performance:** Incentives should be proportional to the returns delivered to depositors. This goal is built around four key elements:

- **Long-term focus:** Reward consistent performance over many years.
- **Risk-return balance:** Encourage prudent risk-taking to make it easier to produce sustainable, long-term returns for depositors, taking into account their risk tolerance.

- **Overall assessment:** Strike a balance between individual, portfolio and Caisse performance.
- **Emphasis on Caisse perspective:** Increased weighting of employees' contribution in supporting the Caisse's strategic priorities and contributing to its overall performance, including an increased weight on leadership and desired behaviours.

**2. Offer competitive compensation:** Attract, motivate and retain employees with experience and expertise consistent with the Caisse's strategic objectives, respecting the guidelines contained in the Regulation Regarding Internal Management presented in the previous section.

**3. Link the interests of executives and depositors:** Ensure that they orient their individual and team efforts toward the Caisse's long-term, sustainable success.

This goal has been translated into a deferred and co-invested incentive compensation mechanism, established in 2010 and mentioned on page 108 of this Annual Report.

Finally, the Caisse's incentive compensation policies comply with the Principles for Sound Compensation Practices issued by the Financial Stability Forum (FSF) and endorsed by G20 nations, effective compensation governance, an alignment between compensation and long-term, prudent risk-taking and regular review of compensation practices.

#### **Total compensation components**

For the Caisse's employees, total compensation is based on four components:

1. Base salary
2. Incentive compensation
3. Pension plan
4. Benefits

1. For compensation purposes, the first quartile ranges from the 1<sup>st</sup> to 25<sup>th</sup> percentile, the second quartile from the 26<sup>th</sup> to 50<sup>th</sup> percentile, the third quartile from the 51<sup>st</sup> to the 75<sup>th</sup> percentile and the fourth quartile from the 76<sup>th</sup> to 100<sup>th</sup> percentile.

## Report of the Human Resources Committee

### Base salary

The Regulation Respecting Internal Management states that the average base salary must not exceed the midpoint of the salary ranges. Within these parameters, the annual base salaries are set according to prevailing reference market salary conditions. Furthermore, the base salaries of certain employees may have been adjusted during the year to reflect significant changes in responsibilities or due to exceptional circumstances. Each year, the Human Resources Committee submits the payroll budget to the Board for approval.

For 2011, the Caisse's management recommended that the Board approve:

- A salary scale freeze for all positions.
- A senior executive salary freeze.
- A 1.6% merit increase in the payroll budget, which is below the median of the market increase forecasts.

### Incentive compensation

In the investment community, incentive compensation is an essential component of the compensation package for employees in this sector because it aligns financial incentives with the performance targets of clients.

Incentive compensation at the Caisse serves to recognize performance, objective achievement and efforts to execute strategic guidelines. The Regulation Respecting Internal Management positions total compensation in the top 10 percent (90<sup>th</sup> percentile) of the

reference markets for investment duties or the third quartile (75<sup>th</sup> percentile) of the reference markets for non-investment duties. Incentive compensation is an essential part of total compensation. It has a direct influence on the total compensation level and its position relative to the reference market.

It should also be noted that, from 2010 to 2012, limits will be applied on incentives that can be paid under the Caisse's new incentive compensation program, which came into effect last year. The purpose of this interim measure is to ensure that the objective of the program, which is to reward the long-term performance of employees, is respected.

Performance incentives are never guaranteed. They depend on the evaluation of performance criteria, as established by the incentive compensation program. Accordingly, employees receive performance incentives based on the three factors outlined in Figure 52.

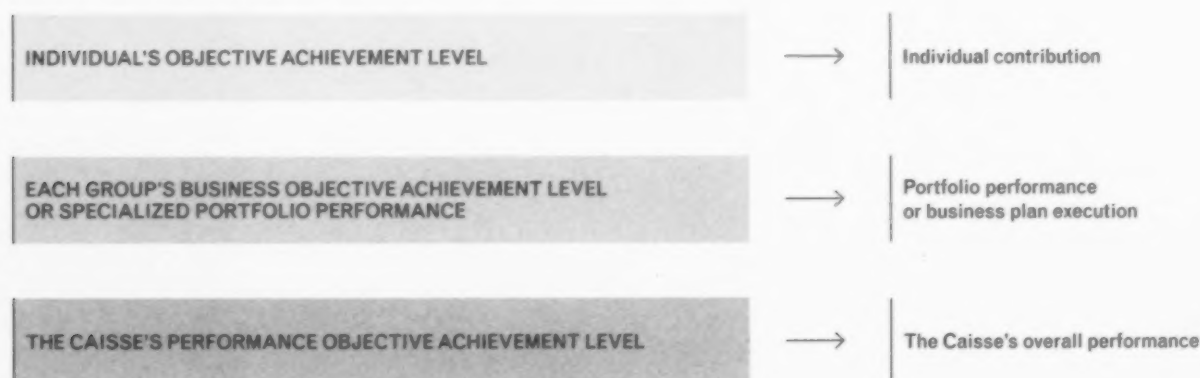
### 2010 achievements

In 2010, the Caisse generated a positive absolute return of 13.6%, which represents:

- An outperformance that exceeds the benchmark index by 4.1%, generating \$5,084 million of added value in 2010, continuing a trend that began in the second half of 2009.
- A return that compares favourably to the performance of peers, according to RBC Dexia data.

FIGURE 52

## PERFORMANCE INCENTIVE FACTORS



Nine of the 11 actively managed portfolios outperformed their benchmark index or added value. In several cases, including the Bonds, Real Estate Debt, Infrastructure, Real Estate and Private Equity portfolios, portfolio performance was achieved despite a tighter management framework and decreased risk.

In addition, the Caisse also achieved other key strategic objectives of its business plan:

- Refocused its investment strategies on the Caisse's core businesses and significantly changed its portfolio offering to make it more flexible and better meet the needs of depositors (by creating three portfolios and changing the mandates of 11 other portfolios).
- Maintained a balance between performance and risk, as shown in the Risk Management section on pages 50 to 62, including:
  - 10% reduction in the Caisse portfolio's absolute risk and a decrease of over 50% in its active risk since December 31, 2009.
  - Maintained a robust liquidity level.
  - Further reduced overall leverage ratio by more than 25% (total liabilities vs. assets) in 2010.
- Completed an \$8 billion refinancing in June, which helped further improve the Caisse's balance sheet. This financing was used to repay short-term debt and better match financing sources and financed real estate assets. This financing did not increase the Caisse's leverage.
- Implemented several initiatives to strengthen the Caisse's leadership in Québec (see the Contribution to Québec Economic Development section on pages 65 to 84).
- Established a new operational business model (including the Operations and Information Technology sectors) focused on the client and efficiency, generating annual recurring savings of \$25 million.
- Reduced operating expenses and management fees to \$269 million. The operating expenses-to-total assets ratio decreased from 22 cents to 19.4 cents per \$100 of assets from 2009 to 2010, a level that compares favourably to best-in-class manager standards (see Table 64 on page 128).

#### 2010-2012 transition period

Although the Regulation Respecting Internal Management allows superior performance to be rewarded by total compensation up to the top 10 percent (90<sup>th</sup> percentile) or the third quartile (75<sup>th</sup> percentile), depending on the positions, the Caisse's incentive compensation program limits the amount of incentives during the three-year transition period, from 2010 to 2012. Indeed, given that this is the first year of the new incentive compensation program, which is structured to cover four years of returns, the Caisse introduced limits on incentive payments possible under the program.

#### 2010 incentives

The limit for incentive payments under the program for 2010 reflects the fact that the program takes into consideration only one year of performance. The program was designed for the long term and, although the 2010 returns are excellent, they were achieved in only one year. Due to the incentive payment limits in 2010, the total compensation of the Caisse's employees is below or near the median in 2010 (see Table 53).

More specifically, a study by Towers Watson indicates that the total compensation of employees ranges between the 40<sup>th</sup> and 55<sup>th</sup> percentile, which positions it, on average, below the market median (48<sup>th</sup> percentile) – despite a performance that compares favourably with the returns of the Caisse's peers. According to RBC Dexia, this performance (13.6%) ranks the Caisse above the first quartile (11.9%) and first 10 percent (13.4%) in 2010 for funds with \$1 billion or more in net assets under management.

TABLE 53

#### 2010 TOTAL COMPENSATION POSITION BY JOB

Positions	Maximum total compensation under the Regulation <sup>1</sup>	Total compensation position
Investment duties	90 <sup>th</sup> percentile	Between the 40 <sup>th</sup> and 55 <sup>th</sup> percentile
Non-investment duties	75 <sup>th</sup> percentile	

1. The maximum total compensation refers to the parameters established by the Regulation Respecting Internal Management.

## Report of the Human Resources Committee

The opinion of Hugessen Consulting presented to the Caisse's Board of Directors points out:

*"We reviewed the returns of the Caisse and benchmarks for 2010 as well as the origin of the Caisse's returns – and we are satisfied. The value-added and return multiple calculations are consistent with the Caisse's compensation program. In our opinion, the total amount of incentives determined by the program in 2010 is very reasonable based on market conditions, considering the Caisse's performance in 2010."*

### Deferred and co-invested performance incentives

To strike a balance between short and long-term incentive compensation based on financial sector practices in this respect, the program makes it mandatory to defer a minimum of 40% of total incentive compensation for senior executives and, during the transition period that ends in 2012, 25% of that for executives and investors in a co-investment portfolio.

The co-investment portfolio aims to better align the long-term interests of employees with the most influence on the Caisse's organizational and financial performance, and those of the depositors. The value of the deferred and co-invested performance incentive amounts will vary – upward or downward – with the Caisse's overall mean absolute returns during the incentive deferral period.

At the end of each three-year period, the deferred amount, plus or minus the performance credit for the period, will be paid to each participant as a restricted incentive payment (see Figure 54).

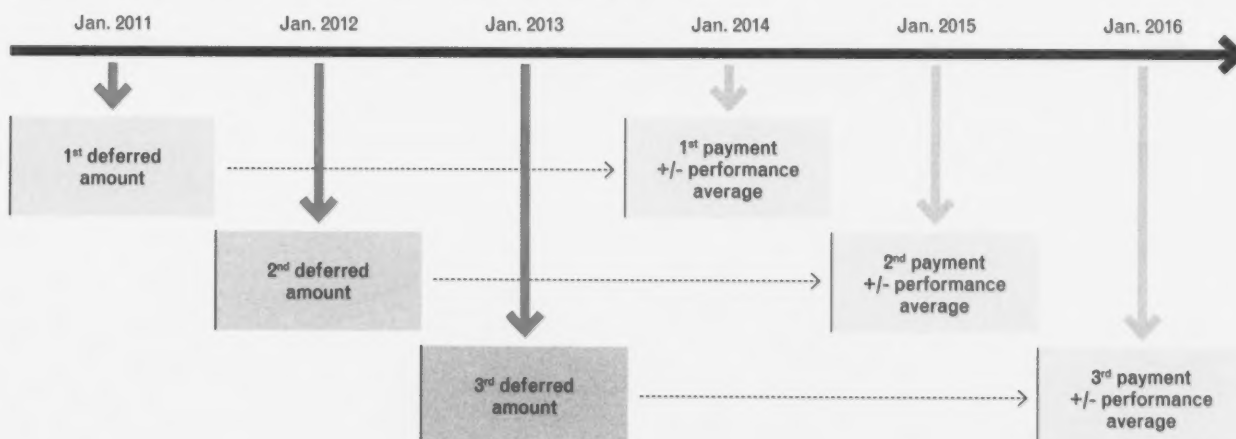
Senior executives have three years to contribute at least the equivalent of their base salary into the co-investment account.

### Pension plan

All employees participate and contribute to one of two defined benefit pension plans – either the Government and Public Employees Retirement Plan (RREGOP) or the Pension Plan for Management (RRPE), depending on their position. In addition, senior executives participate in the Supplemental Pension Plan for Designated Officers (RSRCD). Under both plans, these executives are entitled to receive, after the normal age of retirement, a total annual pension equal to 2% of their eligible earnings for each year or fractional year of plan participation, taking into account the annual fiscal limits imposed by the Canada Revenue Agency for each year they were not RSRCD members. Some senior executives will be granted additional years of service to RSRCD, depending on the particular circumstances of their hiring or promotion. No changes were made to the plan in 2010.

FIGURE 54

### DEFERRED AND CO-INVESTED PERFORMANCE INCENTIVES



### **Benefits**

Employees enjoy a range of competitive benefits, including group insurance (such as medical, dental and life insurance). Moreover, senior executives enjoy fringe benefits that mainly cover the costs associated with car allowances. The Caisse also requires its officers to get yearly health checkups. No changes were made to benefit plans in 2010.

### **President and CEO's performance and total compensation review**

#### **Performance review**

In early 2010, the Committee recommended a series of detailed objectives, proposed by the President and CEO, to the Board for approval. The objectives fall along these five lines:

- Carry out the strategic plan's five priorities.
- Ensure that the Caisse's portfolio remains sufficiently flexible in a volatile and uncertain environment.
- Consolidate the Caisse's financial position in terms of liquidity, asset-liability matching and leverage reduction.
- Improve organizational effectiveness by changing the business model, particularly in the sectors of operations, information technology and human resources.
- Develop an integrated talent management plan to align human resources management practices with strategic priorities.

The President and CEO reported on his achievements to the Chairman of the Board who, in turn, made his report to the Committee in charge of evaluating them. At the end of the process, a report was submitted to the Board of Directors, stating:

*"The President and Chief Executive Officer agreed earlier this year to be judged on a set of detailed and very demanding objectives. They were met and exceeded many times. Therefore, we recognize his outstanding performance."*

The Board of Directors ruled that the achievements of the President and CEO had far exceeded targets, particularly in terms of depositor relationships, performance, financial results, risk management, integrated talent management and the deployment of the strategic priority action plan.

#### **Total compensation review**

The compensation and other employment conditions for the President and CEO are based on the parameters set by the Government in consultation with the Board of Directors. In accordance with Mr. Sabia's intent to waive any pay increase for two years, his annual base salary was maintained at \$500,000. The other employment conditions to which Mr. Sabia has a right are aligned with the Caisse's policies and comply with its Regulation Respecting Internal Management. He received \$40,000 in annual fringe benefits and participated in the Caisse's Employee Group Insurance Plan. Upon his appointment, Mr. Sabia waived participation in the 2009 and 2010 incentive compensation programs.

For the duration of his mandate, Mr. Sabia waived participation in any pension plan. He also waived severance pay, whatever the cause. However, given mandatory participation in the Basic Pension Plan for Management under the provisions of the Pension Plan for Management (based on CARRA rules), Mr. Sabia must participate despite his waiver. The mandatory plan represented an annual cost of \$13,145 to the Caisse in 2010.

In 2010, the total compensation of the President and CEO trailed the market, in comparison with his peers from eight pension funds that are part of the reference market. For superior performance, a gap of about \$3.7 million exists between the total compensation of the President and CEO and his peers.

#### **Summary of the compensation of the President and CEO and the five most highly compensated senior executives for 2008-2010**

The Caisse's Board of Directors recognizes the importance of qualified leadership and firmly believes that its endorsed policies and programs:

- Provide competitive compensation to its senior executives in a fiercely competitive market for talent, where the Caisse is competing globally to generate expected returns.
- Achieve the strategic objectives that help fulfill the Caisse's mission.

Below, in accordance with the Act respecting the Caisse de dépôt et placement du Québec, the Caisse discloses the compensation of the President and CEO and the five most highly compensated senior executives under his direct authority (see Table 58). This disclosure was made for both the Caisse and its wholly owned subsidiaries.

# Report of the Human Resources Committee

TABLE 55

## REFERENCE MARKET – INVESTMENT DUTIES

### INSURANCE COMPANIES

- AEGON Canada
- AXA Canada
- Canada Deposit Insurance Corporation
- Canadian Medical Protective Association
- Independent Order of Foresters
- Industrial Alliance Insurance and Financial Services
- Insurance Corporation of British Columbia
- Intact Investment Management
- Sun Life Financial Services of Canada
- The Great-West Life Assurance Company
- Workers' Compensation Board of Alberta
- Workplace Safety and Insurance Board (Ontario)

### PENSION FUNDS

- Air Canada Pension Plan
- Alberta Investment Management Corporation
- Bimcor
- British Columbia Investment Management Corporation
- Canada Post Pension Plan
- Canadian Broadcasting Corporation Pension Plan
- City of Edmonton
- Civil Service Superannuation Board (Manitoba)
- CN Investment Division
- CPP Investment Board
- Halifax Regional Municipality Pension Plan
- Healthcare Employees' Pension Plan (Manitoba)
- HOOPP (Healthcare of Ontario Pension Plan)
- Hydro-Québec
- New Brunswick Investment Management Corporation
- Nova Scotia Pension Agency
- OMERS (Ontario Municipal Employee Retirement System)
- OPSEU Pension Trust
- Ontario Pension Board
- Ontario Teachers' Pension Plan Board
- Pension Plan of the Société de transport de Montréal
- Public Sector Pension Investment Board (PSP Investments)
- Régime de rentes des policiers et policières de la Ville de Montréal
- TELUS Corporation (pension plan)
- University of British Columbia Investment Trust

### INVESTMENT ADVISERS – WITHOUT PARENT COMPANY

- ATB Financial
- Cardinal Capital Management
- Connor, Clark & Lunn Financial Group
- Fiera Capital
- Greystone Managed Investments Inc.
- Guardian Capital LP
- Jones Collombin Investment Counsel Inc.
- Leith Wheeler Investment Counsel
- Matrix Asset Management Inc.
- Mawer Investment Management Ltd.
- McLean & Partners
- Nexus Investment Management
- Picton Mahoney Asset Management
- Professionals' Fund Group
- Sionna Investment Managers
- Pembroke Management Limited
- Tetrem Capital Partners

### INVESTMENT ADVISERS – WITH PARENT COMPANY

- Desjardins Asset Management
- MD Financial
- TD Asset Management
- NATCAN Investment Management Inc.
- HSBC Global Asset Management (Canada)
- RBC Global Asset Management

TABLE 56

## REFERENCE MARKET – NON-INVESTMENT DUTIES

- |   |                                |  |
|---|--------------------------------|--|
| • AbitibiBowater                        | • Cogeco                       | • Molson Canada  |
| • Accenture                             | • Desjardins Group             | • Power Corporation of Canada                              |
| • Agropur, Cooperative                  | • Domtar                       | • Pratt & Whitney Canada                                   |
| • Air Canada                            | • Ericsson Canada              | • Public Sector Pension Investment Board (PSP Investments) |
| • AkzoNobel Canada                      | • Gaz Metro                    | • Rio Tinto Alcan  |
| • Alcoa Canada                          | • GE Canada                    | • SNC-Lavalin  |
| • AstraZeneca Canada                    | • Gesca                        | • Société des alcools du Québec                            |
| • AXA Canada                            | • GLV                          | • Standard Life Canada                                     |
| • Bank of Montreal                      | • Hydro-Québec                 | • Tembec   |
| • BCE                                   | • IBM Canada                   | • The Great-West Life Assurance Company                    |
| • Bell Helicopter Textron Canada        | • Imperial Tobacco Canada      | • Transat A.T.   |
| • Bombardier Aerospace                  | • Intact Financial Corporation | • UAP  |
| • Bombardier                            | • Lafarge Canada               | • Videotron  |
| • Bombardier Transportation             | • Laurentian Bank of Canada    | • World Color Press  |
| • Cadillac Fairview Corporation Limited | • Lombard Canada               | • Yellow Media   |
| • Canadian Broadcasting Corporation     | • Loto-Québec                  |  |
| • CGI Group                             | • Merck Frosst Canada          |  |

TABLE 57

## REFERENCE MARKET – PRESIDENT AND CEO

- |  |  |  |
|--|--|--|
| • Alberta Investment Management Corporation          | • CPP Investment Board                                 | • Ontario Teachers' Pension Plan Board                     |
| • Bimcor   | • HOOP (Healthcare of Ontario Pension Plan)            | • Public Sector Pension Investment Board (PSP Investments) |
| • British Columbia Investment Management Corporation | • OMERS (Ontario Municipal Employee Retirement System) |  |

# Report of the Human Resources Committee

TABLE 58

## SUMMARY OF THE COMPENSATION OF THE PRESIDENT AND CEO AND THE FIVE MOST HIGHLY COMPENSATED SENIOR EXECUTIVES FOR 2008-2010

Name and main position	Fiscal year	Salary (\$)	Incentive compensation <sup>1</sup> (\$)	Other compensation (\$)	Direct compensation <sup>2</sup> (\$)	Pension plan's value <sup>3</sup> (\$)
Michael Sabia President and CEO <sup>4</sup>	2010	500,000	N/A	40,000	540,000	N/A
	2009	403,846	N/A	32,308	436,154	N/A
Roland Lescure Executive Vice-President and Chief Investment Officer	2010	450,000	780,000	30,000	1,260,000	179,200
	2009	110,769	N/A	407,385	518,154	29,100
Normand Provost Executive Vice-President, Private Equity and Chief Operations Officer	2010	362,885	712,500	30,000	1,105,385	307,600
	2009	348,558	300,000	28,365	676,923	234,300
	2008	325,000	0	25,000	350,000	108,200
Daniel Fournier President, Real Estate group and Executive Vice-President, Real Estate <sup>5</sup>	2010	195,330	420,000	313,022	928,352	191,200
Claude Bergeron Executive Vice-President and Chief Risk Officer <sup>6</sup>	2010	329,066	325,000	296,667	950,733	214,700
	2009	305,177	350,000	25,038	680,215	237,200
	2008	275,000	0	20,000	295,000	77,934
Bernard Morency Executive Vice-President, Depositors and Strategic Initiatives <sup>7</sup>	2010	375,000	250,000	280,000	905,000	180,200
	2009	136,250	300,000	301,762	738,012	32,900

1. As mentioned on page 108 of this report, senior executives must defer a minimum of 40% of their total incentive compensation in a co-investment portfolio, as required by the incentive compensation program. In 2013, senior executives will be eligible to receive a deferred and co-invested incentive payment increased or decreased by the Caisse's mean absolute return. The amounts deferred and co-invested until 2013 regarding 2010 equal to \$520,000 for Mr. Lescure, \$487,500 for Mr. Provost, \$300,000 for Mr. Fournier, \$325,000 for Mr. Bergeron and \$375,000 for Mr. Morency.

2. The direct compensation value includes the salary, incentive compensation and other compensation. It excludes the value of pension plan.

3. The pension plan's value equals the present value of the pension benefits earned during the year and any compensatory change that occurred during the year. This value corresponds to the variation due to compensatory items, as presented in Table 59: Pension Summary of the President and CEO and the five most highly compensated senior executives.

4. Upon his appointment, Mr. Sabia waived his participation in any incentive compensation program for 2009 and 2010. In addition, he waived participation in any pension plan for the duration of his mandate. However, participation in the Pension Plan for Management is mandatory under CARRA rules. For details, visit [http://www.carra.gouv.qc.ca/ang/regime/rrpe/rrpe\\_s03.htm](http://www.carra.gouv.qc.ca/ang/regime/rrpe/rrpe_s03.htm).

5. Mr. Fournier was appointed President, Real Estate group and Executive Vice-President, Real Estate, in July, 2010. He received a lump-sum indemnity staggered over several years as compensation for money he had to waive upon ceasing his previous activities. This amounted to \$300,000 in 2010.

6. Mr. Bergeron was appointed Executive Vice-President and Chief Risk Officer in November 2010. In recognition of his past and ongoing contribution to the active management and restructuring of the ABTN file, he received a lump-sum of \$266,667 in 2010.

7. Mr. Morency received a lump-sum indemnity, staggered over several years, as compensation for professional fees that he had to waive when he was hired and ceased his consulting activities with clients other than the Caisse. This amounted to \$250,000 in 2010.

TABLE 59

# **PENSION SUMMARY OF THE PRESIDENT AND CEO AND THE FIVE MOST HIGHLY COMPENSATED SENIOR EXECUTIVES**

Name and main position	Years of credited service <sup>1</sup>	Annual benefits <sup>2</sup> (\$)		Accrued obligation at start of year <sup>3</sup> (\$)	Variation due to compensation items <sup>4</sup> (\$)	Variation due to non-compensation items <sup>5</sup> (\$)	Accrued obligation at year-end <sup>3</sup> (\$)
		At year-end	At age 65				
Michael Sabia President and CEO <sup>6</sup>	1.8	4,500	23,800	0	0	0	0
Roland Lescure Executive Vice-President and Chief Investment Officer	1.2	44,600	315,000	43,200	179,200	110,200	332,600
Normand Provost Executive Vice-President, Private Equity and Chief Operations Officer	30.6	233,400	364,100	954,900	307,600	447,600	1,710,100
Daniel Fournier President, Real Estate group and Executive Vice-President, Real Estate	0.4	15,600	252,300	0	191,200	48,000	239,200
Claude Bergeron Executive Vice-President and Chief Risk Officer	30.2	185,400	262,500	599,800	214,700	223,200	1,037,700
Bernard Morency Executive Vice-President, Depositors and Strategic Initiatives	1.4	24,300	103,100	39,200	180,200	41,600	261,000

1. This is the number of years of credited service in the basic plan.

2. The annual benefits equal the amount of the pension payable under the Basic and Supplemental Plans at the end of the year or 65 years old.

3. The obligations do not include those of the Basic Plan since employer and employee contributions are remitted to CARRA, which assumes the liability for the benefits. The Caisse's contribution was approximately \$13,145 per executive in 2010.

4. The variation is due to compensation items, including the annual cost of pension benefits, base salary changes, plan changes or the awarding of additional years of service.

5. The variation is due to non-compensation items, including interest accrued on the accrued obligation in the beginning of the year, actuarial gains and losses associated with items other than compensation and changes in actuarial assumptions.

6. Mr. Sabia waived participation in any pension plan. However, participation in the Pension Plan for Management is mandatory under CARRA rules.

For details, visit [http://www.carra.gouv.qc.ca/ang/regime/rrpe/rrpe\\_s03.htm](http://www.carra.gouv.qc.ca/ang/regime/rrpe/rrpe_s03.htm).

Report of the Human  
Resources Committee

TABLE 60

**SUMMARY OF SEVERANCE PAY FOR THE PRESIDENT AND CEO  
AND THE FIVE MOST HIGHLY COMPENSATED SENIOR EXECUTIVES**

Name and main position	Precipitating event	Theoretical amount payable (\$)
Michael Sabia President and CEO <sup>1</sup>	Contract termination	0
Roland Lescure Executive Vice-President and Chief Investment Officer <sup>2</sup>	Non voluntary termination	900,000
Daniel Fournier President, Real Estate group and Executive Vice-President, Real Estate <sup>2</sup>	Non voluntary termination	900,000
Normand Provost Executive Vice-President, Private Equity and Chief Operations Officer <sup>3</sup>	Non voluntary termination	395,000
Claude Bergeron Executive Vice-President and Chief Risk Officer <sup>4</sup>	Non voluntary termination	750,000
Bernard Morency Executive Vice-President, Depositors and Strategic Initiatives <sup>5</sup>	Non voluntary termination	500,000

1. No severance pay is payable even if the departure is not voluntary.

2. This executive's employment contract provides severance pay in the event of dismissal without just cause, which equals twice his annual base salary.

3. This executive's employment contract does not include a specific condition related to his employment termination. His termination indemnity severance pay is based on the Caisse's guidelines on the subject, which provides one-month of base salary for each year of service – to a maximum of 12 months.

4. This executive's employment contract provides severance pay in the event of dismissal without just cause, which equals his annual base salary, plus an amount that equals his annual target incentive compensation.

5. This executive's employment contract provides severance pay in the event of dismissal without just cause, which equals \$500,000.

TABLE 61

**BENCHMARKING OF 2010 POTENTIAL MAXIMUM DIRECT COMPENSATION AND CAISSE DIRECT COMPENSATION FOR THE PRESIDENT AND CEO AND THE FIVE MOST HIGHLY COMPENSATED SENIOR EXECUTIVES**

Position	Reference market in accordance with the Caisse Regulation <sup>1</sup>	Caisse	Ratio (%)
	Maximum direct compensation (\$)	Direct compensation in 2010 <sup>2</sup> (\$)	
	(A)	(B)	(B)/(A)
President and CEO <sup>3</sup>	4,187,000	540,000	13
Executive Vice-President and Chief Investment Officer <sup>4</sup>	3,602,000	1,260,000	35
Executive Vice-President, Private Equity and Chief Operations Officer <sup>4</sup>	3,210,000	1,105,385	34
President, Real Estate group and Executive Vice-President, Real Estate <sup>4,5</sup>	3,479,000	928,352	27
Executive Vice-President and Chief Risk Officer <sup>4</sup>	1,494,000	950,733	64
Executive Vice-President, Depositors and Strategic Initiatives <sup>4</sup>	N/A	905,000	N/A

1. As stipulated in the Regulation Respecting Internal Management, potential total compensation at the 75<sup>th</sup> percentile of the reference market was used for the positions of President and CEO and non-investment duties. The 90<sup>th</sup> percentile of the reference market was used for investment duties. These amounts exclude the value of pension plan and include the value of fringe benefits.

2. These amounts include direct compensation paid in 2010, as shown in Table 58.

3. Towers Watson, Compensation of the President and Chief Executive Officer Study, Caisse de dépôt et placement du Québec, 2011.

4. Towers Watson, Compensation of Executive Committee Members Study, Caisse de dépôt et placement du Québec, 2011.

5. Mr. Fournier was appointed President, Real Estate group and Executive Vice-President, Real Estate, in July, 2010.

# Report of the Risk Management Committee

## HIGHLIGHTS

**01** Established new risk-return ratios for each specialized portfolio and the Caisse overall.

**02** Reviewed investment policies of the specialized portfolios to better manage investment and risk activities.

**03** Implemented a new methodology for credit risk measurement.

## THE RISK MANAGEMENT COMMITTEE

The Board of Directors established the Risk Management Committee to assist the Audit Committee with its responsibility of implementing a risk management process.

### MANDATE

The Risk Management Committee:

- Establishes oversight guidelines, policies and bodies – in addition to control systems – to maintain an appropriate level of business, financial and operational risks (and recommends them to the Board).
- Ensures that risks are clearly identified and that an appropriate process is in place to manage them.
- Reviews and submits every investment file for approval under the Integrated Risk Management Policy.
- Ensures that the Caisse fulfills its obligations to the depositors by complying with their investment policies and the investment policies of the specialized portfolios, making any necessary recommendations to the Board.
- Provides the Audit Committee with the necessary information on the implementation of the risk management process.

During the year, the Committee, in collaboration with the Governance and Ethics Committee, reviewed its mandate and that of its Chair.

## COMPOSITION (as at December 31, 2010)

- Chair: Réal Raymond
- Members: Pierre Fitzgibbon, François R. Roy and Ouma Sananikone
- Guest member: A. Michel Lavigne, Chair of the Audit Committee

The Board Chairman regularly attends meetings. Jocelyne Dagenais participated in discussions on the risk management program during the first quarter of 2010.

## REPORT

Number of regular meetings in 2010: 8

The Committee has various mechanisms to provide the Audit Committee and Board with the necessary assurance regarding the implementation of a risk management process. The Committee:

- Provided a verbal and written report on its activities to the Board after each meeting.
- Submitted copies of its minutes to the Audit Committee and the Board.
- Invited the Chair of the Audit Committee to each meeting.

The Committee held meetings regularly without the presence of senior management.

The report below, which describes the issues that were subject to discussions and decisions during the year, was approved by the Committee members.

### Risk management oversight guidelines and policies

- Monitored work on the risk management program, which revolves around four major activities, including the integration of daily risk-return, establishment of new frameworks and processes, improvements to risk management tools and the enhancement of risk-return dialogue:
  - Supported the Risk group with the implementation of a new governance model, including the establishment of risk-return reports for each specialized portfolio and the Caisse overall, which are central to the dialogue between the Risk group and Investment groups.
  - Examined the risk-return reports of an Investment group's specialized portfolios and the risk-return report of the Caisse's overall portfolio, at each Committee.
  - Reviewed the investment policies of the specialized portfolios to better manage investment and risk activities and make recommendations to the Board of Directors for approval.
  - Reviewed, and recommended to the Board, value-added targets and risk limits for the specialized portfolios and their benchmark indexes.
  - Reviewed, and recommended to the Board, certain hedging strategies for the specialized portfolios.
  - Approved transition and action plans in response to the adoption of new investment policies for certain specialized portfolios.
  - Monitored the implementation of a new methodology for credit risk measurement.
  - Discussed the establishment of a new counterparty credit risk analysis process.
  - Analyzed, and recommended to the Board for approval, amendments to the integrated risk management policy, affecting particularly the management of liquidity and credit risk and the risk limit management process for the Caisse's investment activities.
  - Reviewed, and recommended to the Board, a guideline for equity securities lending and borrowing.
- Reviewed, recommended to the Board and monitored certain hedging transactions that reduced the ABTN portfolio's attributable risk – by reducing the effect of market movements.
- Reviewed, recommended to the Board and monitored an underweight strategy in the Equity portfolios due to increased market risk, particularly related to the European crisis.
- Recommended to the Board a risk limit for financial contracts or instruments, in accordance with the requirements of the Regulation related to the determination of instruments or contracts of a financial nature and the framework for their use; receiving periodic reports on compliance based on this limit.

- Discussed the new structure set up by the Risk group and, among other things, reviewed the responsibilities of the two deputy chiefs.
- Reviewed the Risk group's business plan for 2011.
- Received accountability reports on compliance and internal controls.

### Investment files

- Reviewed and recommended investment files under the Board's authority, considering the analysis of the team responsible for the transaction, the project risk analysis and, more specifically, its impact on the risk level and concentration of the specialized portfolio and the Caisse's overall portfolio, as well as the investment's compliance with risk oversight policies and guidelines.
- Discussed the risk-return relationship for each investment file submitted to the Committee.
- Received the report on the monitoring of investment files authorized by the Board and the Caisse's senior management (not falling under the Board's purview).
- Regularly monitored major investments with a particular impact on the risk level and concentration of the specialized portfolio and the Caisse's overall portfolio.

### Depositors

- Analyzed the certificates of compliance with the depositors' investment policies and the investment policies of specialized portfolios.
- Discussed the depositors' expectations about the establishment and monitoring of investment policies.
- Obtained assurance that the depositors have an opportunity to comment on amendments to the investment policies of specialized portfolios.

### USE OF EXTERNAL EXPERT SERVICES

The Risk Management Committee did not use any external expert services in 2010.



# Board of Directors and Executive Committee

# Organizational Structure

The Caisse's Board of Directors consists of the Chairman, President and Chief Executive Officer, depositors' representatives and independent members. The Act respecting the Caisse stipulates that at least two-thirds of the directors, including the Chairman, must be independent.

The Executive Committee is composed of the President and Chief Executive Officer, and senior executives from the Caisse's various sectors. As at December 31, 2010, the Caisse had a total of 741 employees. At this same date, the Real Estate group had 1,932 employees.

FIGURE 62

## ORGANIZATIONAL STRUCTURE – CAISSE

(as at December 31, 2010)

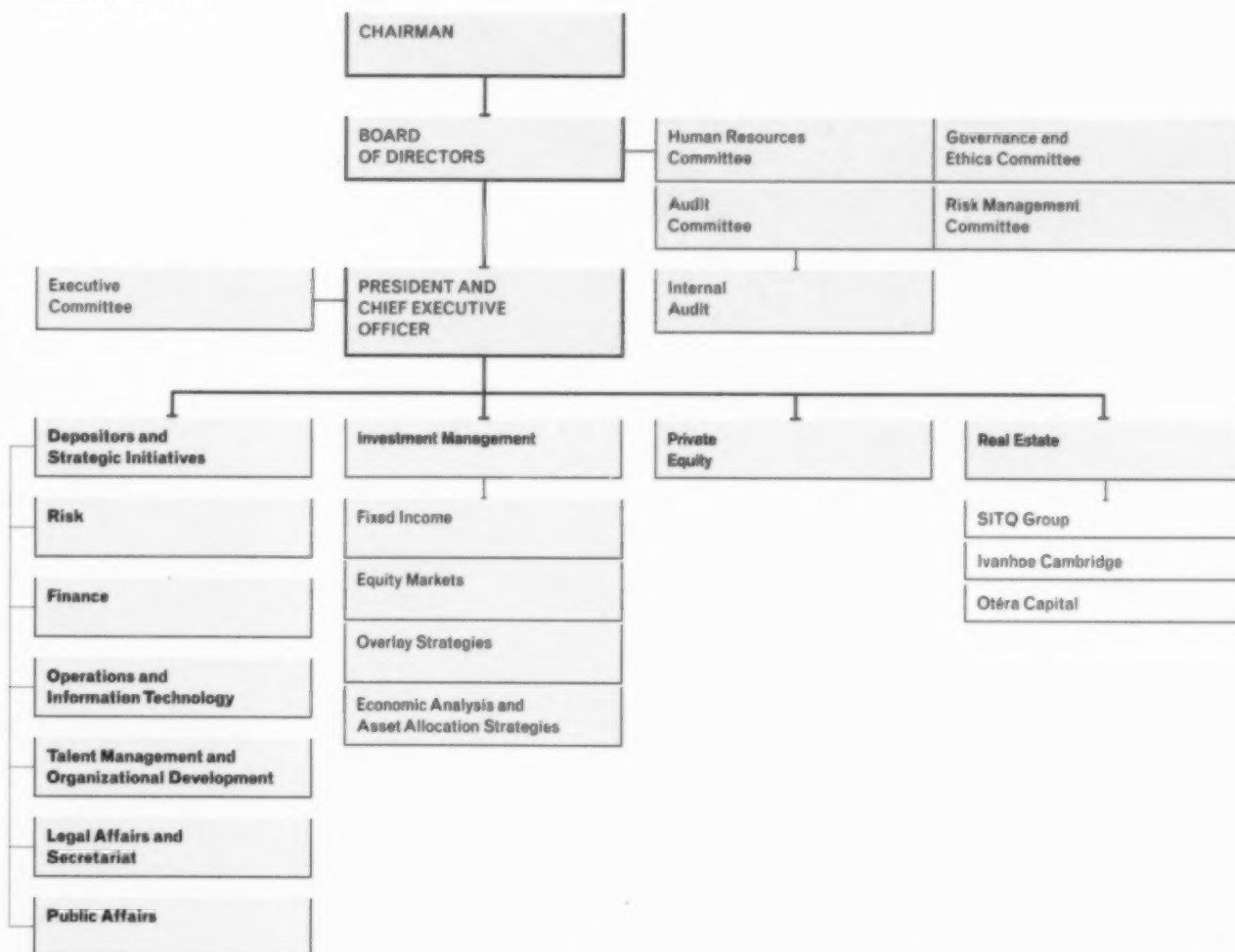
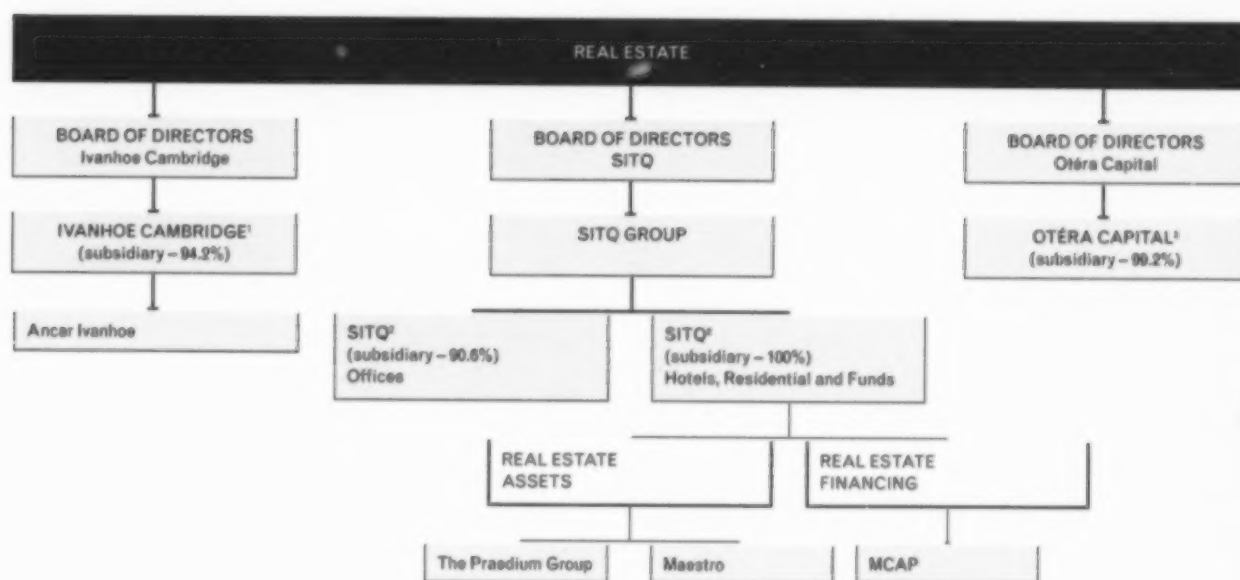


FIGURE 63

## ORGANIZATIONAL STRUCTURE – REAL ESTATE

(as at December 31, 2010)



1. Kim McInnes, President and Chief Executive Officer, Ivanhoe Cambridge

2. William R.C. Tresham, President and Chief Executive Officer, SITQ

3. Ross Brennan, President and Chief Executive Officer, Otéra Capital

## REAL ESTATE SECTOR

The Real Estate group makes equity and debt investments in the offices, business parks, retail, hotels and multi-residential sectors in the Americas, Europe and Asia.

The group is composed of Ivanhoe Cambridge, SITQ Group and Otéra Capital (see Figure 63). Its activities are split into two portfolios: Real Estate and Real Estate Debt.

For more details on the Real Estate sector, visit [www.lacaisse.com](http://www.lacaisse.com).

# Members of the Board of Directors

## ELISABETTA BIGSBY

Corporate Director

**Chair of the Human Resources Committee  
Board member since November 4, 2009**

Elisabetta Bigsby pursued her career at the Royal Bank of Canada from 1977 to 2007, where she was notably a member of the Executive Committee and the Chief Human Resources Officer. She also sat on the Bank's Pension Plan Committee from 1989 to 2007. She currently serves as a corporate director and advises companies on leadership development in cooperation with the International Consortium for Executive Development Research, in Massachusetts. She is also a past director of a number of organizations.

## CLAUDETTE CARBONNEAU

President

Confédération des syndicats nationaux

**Member of the Governance and  
Ethics Committee  
Board member since September 25, 2002**

Claudette Carboneau holds a bachelor's degree in political science and is the first woman to serve as President of the Confédération des syndicats nationaux (CSN), a position she has held since 2002. She is also Chair of Fondation and Vice-President of the General Council of the International Trade Union Confederation, as well as First Substitute of the Canadian delegation to the ITUC General Council. Ms. Carboneau is also a member of the Québec government's Advisory Council on Labour and Manpower.

## LOUISE CHARETTE

Corporate Director

**Member of the Governance and Ethics  
Committee and Audit Committee  
Board member since April 27, 2005**

Louise Charette holds a master's degree in business administration and a doctorate in mathematics. From 1981 to 2007, she occupied various management positions at the Commission de la construction du Québec, including Assistant Director General, Administration and Finance. In addition to her duties as Assistant Director General, she headed the Investment Committee for more than ten years. Ms. Charette has also devoted her talents to a number of organizations. She was a founding member of the Regroupement des femmes cadres du Québec and served as Vice-Chair of the Société d'habitation du Québec. Ms. Charette has been active with not-for-profit organizations for several years and sits on the Advisory Board of the Autorité des marchés financiers.

## JOCELYNE DAGENAI

President and Chief Executive Officer  
Commission administrative des régimes  
de retraite et d'assurances

**Board member since January 1, 2008**

Jocelyne Dagenais has been President and Chief Executive Officer of the Commission administrative des régimes de retraite et d'assurances (CARRA) since December 3, 2007. She has worked for the Québec public sector since 1977. Ms. Dagenais has held various positions, including Deputy Minister and Assistant Deputy Minister, with several ministries. She has also been a member of many boards of directors, including those of Services Québec, the Centre des services partagés du Québec, the Régie de l'assurance maladie du Québec and Canada Health Infoway.

## MICHÈLE DESJARDINS

President, Koby Consulting  
Senior Associate, Lansberg Gersick &  
Associates LLC and Niagara Institute

**Member of the Governance and  
Ethics Committee  
Board member since December 21, 2009**

After a career in the pulp and paper industry with Abitibi-Price and InterCity Papers, Michèle Desjardins held various positions with Price Waterhouse and the Commission des valeurs mobilières du Québec. She subsequently headed the Family Business Institute. For more than a decade, she has served as Senior Associate at Lansberg Gersick & Associates LLC and the Niagara Institute, as well as President of Koby Consulting. Ms. Desjardins is a Certified Management Consultant, a member of the Ordre des administrateurs agréés du Québec and a Certified Corporate Director. She currently sits on the board of the Société du Palais des congrès de Montréal.

## PIERRE FITZGIBBON

President and Chief Executive Officer,  
Atrium Innovations

**Member of the Audit Committee and  
Risk Management Committee  
Board member since April 22, 2009**

Pierre Fitzgibbon has a background in the financial, manufacturing, health and telecom sectors. He has been the President and Chief Executive Officer of Atrium Innovations since 2007 and has also worked with such organizations as the National Bank of Canada group, the Telesystem group's international operations, Domtar, Peerless Carpet Corporation and Price Waterhouse. Mr. Fitzgibbon currently sits on the Board of Directors of Transcontinental. He is a past Chairman of the Board of Cylis and a past director of several companies operating in the technology, telecom and financial services sectors, as well as a number of charitable organizations.

**A. MICHEL LAVIGNE**

Corporate Director

**Chair of the Audit Committee**  
**Guest Member of the**  
**Risk Management Committee**  
**Board member since April 27, 2005**

A. Michel Lavigne was President and Chief Executive Officer of Raymond Chabot Grant Thornton until 2005. He was also Chairman of Grant Thornton Canada and a director of Grant Thornton International. He is Chairman of Teraxion and Primary Energy Recycling and his directorships include Quebecor Media, TVA and Postes Canada. Mr. Lavigne has received many distinctions; most notably, he is a Fellow of the Ordre des comptables agréés du Québec.

**JEAN PIERRE OUELLET**Corporate Director  
Advisor, Capital Saint-Laurent

**Member of the**  
**Human Resources Committee**  
**Board member since March 6, 2009**

Jean Pierre Ouellet has been an advisor to Capital Saint-Laurent since 2008. His past positions include Senior Partner at the Montréal law firm of Stikeman Elliott and Senior Vice-President, Chief Legal Officer and Corporate Secretary of Canadian National Railway. More recently, he served as Vice-Chairman of RBC Capital Markets, with responsibility for Québec. He has been a director of GBO since 2002 and currently chairs its audit committee. He is also a member of the board of Richmond Mines and the Noranda Income Fund, Chair of the Governance and Ethics Committee. Mr. Ouellet is also a member of the advisory board of Talisman Energy. He is a past director of a number of Canadian companies, including Bionair, Hartco Enterprises, C-Mac and Crédit commercial de France (Canada), as well as several non-profit organizations.

**RÉAL RAYMOND**

Corporate Director

**Chair of the Risk Management Committee**  
**Board member since March 13, 2009**

During Réal Raymond's 37-year career with National Bank of Canada, he held a variety of positions including President – Personal and Commercial Banking, President and Chief Operating Officer and, finally, President and Chief Executive Officer. He currently sits on the boards of Metro, Héroux-Devtek, Aéroports de Montréal and the Institute for Research in Immunology and Cancer of the Université de Montréal. Mr. Raymond has an MBA from the Université du Québec à Montréal (UQAM) and currently serves as its chancellor. He holds an honorary doctorate from the UQAM School of Management (ESG UQAM).

**FRANÇOIS R. ROY**

Corporate Director

**Member of the Risk Management Committee**  
**and Audit Committee**  
**Board member since December 21, 2009**

François R. Roy began his career at The Bank of Nova Scotia, where he held several positions in Canada and the United States. He then worked for Société générale de financement du Québec, before becoming the Chief Financial Officer at Quebecor, Avenir and Telemedia Corporation. He has been a corporate director since 1998 and sits on the boards of Transcontinental, Fibrek Noranda Income Fund and Macquarie Power & Infrastructure Income Fund. He was McGill University's Chief Financial Officer from 2007 to 2010. Mr. Roy has been and continues to be active with many not-for-profit organizations over the past 25 years.

**MICHAEL SABIA**President and Chief Executive Officer,  
Caisse de dépôt et placement du Québec

**Board member since March 14, 2009**

Michael Sabia has been the President and Chief Executive Officer of the Caisse since March 2009. Prior to joining the Caisse, he was President and Chief Executive Officer of BCE and CFO of Canadian National Railway. Earlier in his career, he was a senior official in the Government of Canada. Mr. Sabia is very active in the community and he is currently serving as the co-chair of the Grand Bal des Vins-Coeurs for the Montréal Heart Institute Foundation. In recent years, his endeavours have included chairing the fundraising campaign for Maison Saint-Gabriel and co-chairing the campaign for the Montréal Heart Institute Foundation. In 2006, he has co-chaired the campaign for Centraide du Grand Montréal. Mr. Sabia was also a member of the North American Competitiveness Council from 2005 to 2008.

**OUMA SANANIKONE**

Corporate Director

**Member of the Risk Management Committee**  
**and Human Resources Committee**  
**Board member since August 28, 2007**

Ouma Sananikone is a corporate director with extensive experience on the European and Asian financial markets. She has worked for 25 years in banking, financial services and investment management. She is Chairman of Smarte Carte International and a non-executive director of Icon Parking Systems and Air-Serv. Ms. Sananikone has been a board member of numerous public and private companies, as well as charitable organizations, in Australia and elsewhere. Her special areas of interest are governance, ethics, community and leadership.

## Members of the Board of Directors

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### ROBERT TESSIER

Chairman of the Board

**Chair of the Governance and  
Ethics Committee**

**Member of the**

**Human Resources Committee**

**Board member since March 5, 2009**

Robert Tessier has an extensive background as a corporate director and senior executive in both the public and the private sector. He has served as President and Chief Executive Officer as well as Chairman of the Board of Gaz Métro and as the head of Marine Industries Limited and Alstom Canada. He has also been Secretary of the Conseil du trésor du Québec, Québec's Deputy Minister of Energy and Natural Resources and Executive Vice-President of the Société générale de financement du Québec. Currently, Mr. Tessier is Chair of the IG Funds Independent Review Committee and a member of the board of AXA Canada. He also sits on the boards of several other organizations.

### ANDRÉ TRUDEAU

President and General Manager,  
Régie des rentes du Québec

**Board member since January 1, 2008**

André Trudeau is a career public servant with more than 35 years of experience with the Québec government. He is currently President and General Manager and Chairman of the Board of the Régie des rentes du Québec. Prior to this, he served as President and General Manager, Deputy Minister and Associate General Secretary of nearly a dozen government ministries and agencies, including the Ministère du Conseil exécutif, the Ministère de l'Environnement, the Ministère des Affaires municipales, the Ministère des Transports, the Ministère de la Santé et des Services sociaux and the Ministère de l'Emploi et de la Solidarité sociale. Mr. Trudeau's versatility and management skills have been the hallmarks of his career and in 2005 earned him the Prix Hommage awarded by the Institut d'administration publique du Québec.

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# Executive Committee

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## CLAUDE BERGERON

### Executive Vice-President and Chief Risk Officer

Since November 1, 2010, Claude Bergeron oversees the teams responsible for monitoring, measuring and analyzing risk at the Caisse. Mr. Bergeron has more than 20 years of experience with the Caisse where he has played a leading role in a number of major domestic and international files and investments. He became Acting Chief Risk Officer in August 2009. Under his leadership, the Caisse completed the implementation of an accelerated program to strengthen its risk management practices. Mr. Bergeron is a member of the Québec Bar and the Canadian Bar Association. He completed an international MBA program, specializing in financial services and insurance. He has received many awards during his career, including the Commerce-ZSA Québec Lifetime Achievement Award (2007).

## FRÉDÉRIC CHARETTE

### Executive Vice-President Talent Management and Organizational Development

Frédéric Charette oversees the recruitment, compensation, professional development, payroll, management information and human resources advisory teams. During the course of his career, Mr. Charette has worked both abroad and in Montréal, with firms hiring high-level professionals such as McKinsey & Company and KPMG. Among his many professional achievements, he has participated in expanding McKinsey's organizational development practice in the Asia-Pacific region and served as an executive and consultant in this field for many years, working with numerous worldclass clients in North America and Asia. More recently, he served as Head of People for KPMG Australia, a firm employing over 5,000 professionals. Mr. Charette is a member of the International Positive Psychology Association.

## MARC CORMIER

### Executive Vice-President Fixed Income Investment Management

Marc Cormier oversees the Caisse's fixed income teams and portfolios. He has close to 20 years of experience in the banking and investment industry. After joining the institution in 1997, he held various positions with the fixed income investments team. In addition to his portfolio management duties, he oversaw analytical support services for the Fixed Income and Equity Markets sectors, which he set up once he had implemented the necessary technology solution. During the course of his career, Mr. Cormier has worked for several French financial institutions such as Crédit Lyonnais, in Montréal, and Crédit Commercial de France, in Paris.

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## DENIS COUTURE

### Executive Vice-President, Public Affairs

Denis Couture is responsible for internal and external communications, government relations, public relations and public policy issues management. He has developed solid expertise in the international arena and has spent more than 25 years working with several major Canadian corporations in a wide range of industries. Prior to joining the Caisse, he was Senior Vice-President, Corporate and International Affairs, with Brookfield Asset Management, where he had also headed investor relations and communications. Mr. Couture has a law degree from the Université de Montréal. He currently sits on the Board of Directors of the Canada-India Business Council.

## DANIEL FOURNIER

### Executive Vice-President, Real Estate, and President, Real Estate group

Daniel Fournier oversees the institution's real estate investments, including strategy development and portfolio management and growth. He also manages the operations of the Real Estate group's main companies (Ivanhoe Cambridge, Otéra Capital and SITQ Group) and their network, and serves as their Chairman of the Board. Mr. Fournier has more than 30 years of experience in the business community and a solid background in the real estate industry. He holds a Bachelor of History from Princeton University in the U.S. and a Bachelor of Arts in Jurisprudence from Oxford University in the U.K. Mr. Fournier is very involved in the community and most notably has served as President and Founder of NF Canada, an organization dedicated to helping people living with neurofibromatosis.

## MARIE GIGUÈRE, AD. E.

### Executive Vice-President, Legal Affairs and Secretariat

Since November 1, 2010, Marie Giguère supervises the teams responsible for legal affairs, the corporate secretariat and policies and compliance. She has extensive experience in commercial and corporate law, as well as mergers and acquisitions. She was a partner at Fasken Martineau for many years and held management positions at the Montréal Exchange, Molson Inc. and Otéra Capital, a real estate subsidiary of the Caisse. Ms. Giguère has a bachelor's degree in civil law from McGill University. She is a member of the Québec Bar. She sits on the board of the Douglas Mental Health University Institute and chairs the Institute's foundation. In 2005, she received the Commerce-ZSA career excellence award.

## Executive Committee

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### JEAN-LUC GRAVEL

#### **Executive Vice-President, Equity Markets Investment Management**

Jean-Luc Gravel oversees the equity investment teams covering the Canadian and U.S. markets as well as foreign countries, including emerging markets. He is responsible for developing strategies and exploring new opportunities for all of the Caisse's equity market activities. Mr. Gravel began his investing career as a financial reporter for the investment section of the newspaper *Les Affaires*. He joined the Caisse's Canadian equity team in 2004, after working in the securities market for Gendron Norris, Nesbitt Burns, Newcrest Capital and TD Newcrest Securities. He is a Chartered Financial Analyst (CFA) and a Fellow of the Canadian Securities Institute.

### ROLAND LESCURE

#### **Executive Vice-President and Chief Investment Officer**

Roland Lescure oversees investment strategy, asset allocation and investment research. He supervises equity, fixed-income and hedge funds investments as well as overlay strategies. He also plays a key advisory role for private equity and real estate investments. Mr. Lescure has many years of experience in the investment field, working with such firms as Groupama Asset Management, Natexis, the asset management subsidiary of France's Caisse des Dépôts et Consignations, the French department of finance and the Institut national de la statistique et des études économiques (INSEE). He has taught at the university level and contributed to several initiatives undertaken by France's Council of Economic Advisers. Mr. Lescure graduated from the École Polytechnique and ENSAE. He also earned an M.Sc. in Economics from the London School of Economics.

### BERNARD MORENCY

#### **Executive Vice-President Depositors and Strategic Initiatives**

Bernard Morency supervises the teams responsible for the relations between the Caisse and its 25 depositors and manages the development and implementation of the strategic plan and annual business plans. Mr. Morency joined the Caisse in December 2007, following more than 30 years with Mercer. During this time, he served on Mercer's global executive team, fulfilled a variety of leadership and senior management roles and was called upon to advise a number of leading Canadian private and public corporations. Mr. Morency is a Fellow of the Canadian Institute of Actuaries and the U.S. Society of Actuaries (SOA) and is a member of the Conference Board of Canada and of the board of CIRANO.

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### NORMAND PROVOST

#### **Executive Vice-President, Private Equity and Chief Operations Officer**

Normand Provost oversees the teams that invest in the long-term growth of companies. He supervises investment strategy development and portfolio management and growth, and coordinates the Caisse's network of local and international partners. Mr. Provost has served as the organization's Chief Operations Officer since April 2009. Since September 2009, Mr. Provost has also assumed the leadership of all of the Caisse's initiatives in Québec. He heads the steering committee in charge of these endeavours and supervises the team responsible for business development in the province. He is also the Caisse's lead representative in its various activities throughout Québec. Mr. Provost brings 35 years of industry experience to the table, including 30 with the Caisse, where he created the Private Equity team and portfolios and developed its investment business model. Mr. Provost has touched on every aspect of corporate financing and brought hundreds of transactions to fruition.

### MICHAEL SABIA

#### **President and Chief Executive Officer Acting Chief Financial Officer**

Michael Sabia is responsible for the strategic direction of the Caisse and determines the necessary course of action to fulfill its mission. He is also head of the Executive Committee and sits on the Board of Directors. Prior to joining the Caisse, he was President and Chief Executive Officer of BCE and CFO of Canadian National Railway. Earlier in his career, he was a senior official in the Government of Canada. Mr. Sabia is very active in the community and he is currently serving as the co-chair of the Grand Bal des Vins-Coeurs for the Montréal Heart Institute Foundation. In recent years, his endeavours have included chairing the fundraising campaign for Maison Saint-Gabriel and co-chairing the campaign for the Montréal Heart Institute Foundation. In 2006, he has co-chaired the campaign for Centraide du Grand Montréal. He was also a member of the North American Competitiveness Council from 2005 to 2008.

# Financial Report

# Analysis of Operating Expenses and External Management Fees

Operating expenses represent the Caisse's total portfolio management and administration costs. External management fees are amounts paid to external financial institutions to manage funds on the Caisse's behalf. The institution's operating expenses include expenditures for the management of the specialized Real Estate and Real Estate Debt portfolios. Operating expenses related to the management and administration of real estate assets and mortgages are deducted from real estate investment income and mortgage income, respectively.

For fiscal year 2010, operating expenses totalled \$257 million, a \$7 million increase over 2009. External management fees totalled \$12 million, markedly lower than the \$21 million figure reported in 2009. This decrease is mainly due to the termination of some external management mandates. Fees for external management are claimed as a deduction against investment income.

Operating expenses and external management fees amounted to \$269 million in 2010, down \$2 million or 0.7% from \$271 million in 2009. This represents 19.4 cents per \$100 of average net assets: much lower than the last four years (see Figure 64).

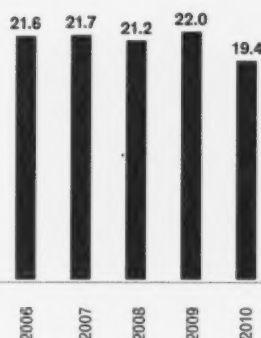
## OPERATIONAL EFFICIENCY

The Caisse periodically reviews its procedures to maintain strict control over its operating expenses. It aims to keep operating expenses at a level that, given the composition of its investments, is favourably comparable to that of same-size institutional fund managers with similar operations. For many years, the Caisse has been benchmarking its costs by asset class. Generally, its total costs compare favourably with those of its peers.

FIGURE 64

### OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES EXPRESSED IN CENTS PER \$100 OF AVERAGE DEPOSITORS' NET ASSETS

(for periods ended December 31 – in cents)



## THE CAISSE'S INITIATIVES TO REDUCE EXPENSES AND INCREASE PRODUCTIVITY

### Budgetary cuts of \$20 M

Following the Québec government's budget in 2010, the Caisse, as part of its action plan to refocus and streamline its activities, implemented a series of measures to reduce its expenses by more than \$20 million. These measures were part of an expenditure control and productivity improvement continuum that began in 2009.

### \$45 M of reduction in expenses or 14% over two years

As a result, over a two year period, operating expenses and external management fees were reduced by \$45 million or 14% from \$314 million in 2008 to \$271 million in 2009 and \$269 million in 2010.

In 2011, the Caisse will continue paying close attention to its expenses in order to keep them as low as possible, making sure to maintain an adequate level of operational resources to fulfill its mandate with the depositors.

# CDP Financial

CDP Financial, a wholly owned subsidiary of the Caisse, enters into financing transactions in local and international institutional markets by issuing commercial paper and term notes. These transactions are aimed at optimizing the financing costs of the Caisse's activities and its subsidiaries, providing greater financing source diversification.

## HIGHLIGHTS

**01** CDP Financial issued term notes with a total value of \$3 billion in the Canadian and European markets.

**02** The \$8 billion financing program was completed in 2010 without an increase in the Caisse's liabilities.

## SHORT-TERM BORROWINGS

CDP Financial entered into short-term financing transactions in the Canadian market, with a fair value of \$1.0 billion as at December 31, 2010, compared to \$1.3 billion as at December 31, 2009 (see Figure 65). The fair value of outstanding commercial paper decreased due to the substitution of short-term debt for longer-term debt. The average maturity of the borrowings was 67 days in 2010, for transactions totalling \$5.5 billion.

In 2010, CDP Financial did not issue any commercial paper in the European market, reflecting a decrease in financing requirements with short-term maturities.

## TERM BORROWINGS

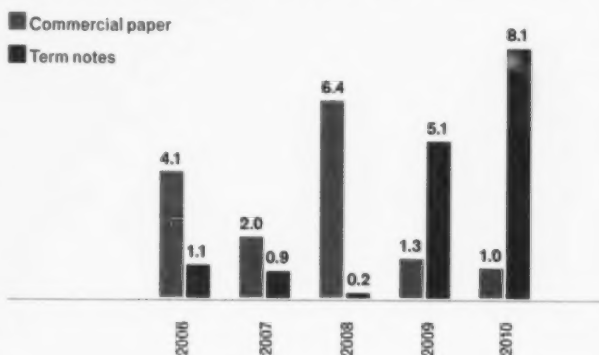
In November 2009, the Caisse authorized an \$8 billion financing program for the purpose of substituting a portion of short-term debt for longer-term debt and better matching financing and financed asset terms. To this end, CDP Financial issued US\$5 billion in term notes in the U.S. market on November 25, 2009.

In 2010, CDP Financial completed the financing program with two subsequent issues. On January 15, 2010, it issued term notes in Canada with a nominal value of \$2 billion, divided into tranches of 5 and 10 years. On June 23, 2010, it issued term notes with a nominal value of €750 million and a maturity of 10 years in the European market (see Figure 66).

FIGURE 65

## BREAKDOWN OF LIABILITIES – CDP FINANCIAL

(fair value as at December 31 – in billions of dollars)

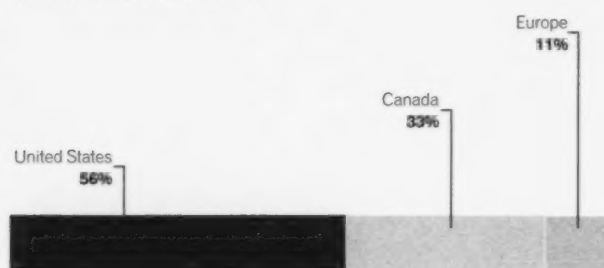


## CDP Financial

FIGURE 66

**GEOGRAPHIC BREAKDOWN OF LIABILITIES –  
CDP FINANCIAL**

(fair value as at December 31, 2010)

**SOLID FINANCIAL FOUNDATIONS**

The \$8 billion refinancing program, completed in June, helped further improve the Caisse's balance sheet. This financing, which was used to repay short-term debt and better match financing sources and financed real estate assets, did not result in any increase in the Caisse's leverage.

In addition, the refinancing program reduced the renewal risk and need for currency hedging, since the term borrowings financed assets denominated in the same currency.

During 2010, credit rating agencies Dominion Bond Rating Service (DBRS), Moody's Investors Service (Moody's) and Standard & Poor's (S&P) maintained their investment grade credit rating with a stable outlook. These credit ratings are the highest issued by these rating agencies (see Table 67).

- On November 17, 2010, Moody's confirmed CDP Financial's short- and long-term credit ratings and maintained a "stable" outlook.
- On October 25, 2010, DBRS issued an update confirming the short- and long-term credit ratings of the Caisse and its subsidiary, CDP Financial, and maintaining a "stable" outlook.
- On November 17, 2010, S&P confirmed the Caisse's short- and long-term credit ratings with a "stable" outlook.

TABLE 67

**CREDIT RATINGS**

	Short-term	Long-term
DBRS	R-1 (HIGH)	AAA
Moody's	PRIME-1 (Aaa)	Aaa
S&P	A-1 + A-1 (HIGH)	AAA

# Critical Accounting Policies

The financial statements of the Caisse de dépôt et placement du Québec are combined: they include the accounts of the Caisse's subsidiaries, General Fund, individual funds and specialized portfolios. Depositors' holdings reported in the Combined Statement of Net Assets reflect the combination of each Caisse depositor's net account value.

Note 2 accompanying the audited Combined Financial Statements as at December 31, 2010 describes the significant accounting policies used by the Caisse. Some of these accounting policies involve subjective and complex judgments and estimates because they concern uncertain matters. Any changes to these judgments and estimates could have a significant impact on the Caisse's Combined Financial Statements.

## CHANGEOVER TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Publicly accountable Canadian companies are required to apply International Financial Reporting Standards (IFRS), in lieu of Canadian generally accepted accounting principles (GAAP), effective January 1, 2011.

The Caisse aims to adopt IFRS for the preparation and presentation of its Combined financial statements. To this end, the Caisse initiated an IFRS adoption program in July 2008. This structured program involves the participation of various Caisse teams, the use of external advisers, employee training and disclosure of the results and impact of these efforts to interested parties.

The Caisse's transition to IFRS is a three-stage process: detailed diagnostics, detailed planning and implementation. The first two stages were completed in 2009. The implementation stage involves mobilizing, coordinating and overseeing various teams to ensure implementation according to expectations and deadlines. The changes will affect accounting processes, business and internal controls, information technology and financial and management reporting. This implementation has already begun and will be completed on time.

In February 2010, the International Accounting Standards Board (IASB) proposed an exemption that would allow investment companies to publish IFRS financial statements without consolidating subsidiaries. These subsidiaries would instead be reported as investments at fair value.

Following this development, in 2010, the Accounting Standards Board (AcSB) decided to provide a one-year deferral of the mandatory IFRS changeover date to investment companies that apply the Accounting Guideline AcG-18, "Investment Companies," of the Canadian Institute of Chartered Accountants (CICA) Handbook.

On January 12, 2011, the AcSB decided to extend by one year the deferral of the mandatory IFRS changeover date for these firms, since the IASB's investment company project has been delayed and a final standard will not likely be issued before January 1, 2012.

Accordingly, the Board Audit Committee, in February 2011, authorized the Caisse to prepare its IFRS-compliant Combined Financial Statements starting on January 1, 2013.

## ADOPTION OF FUTURE ACCOUNTING STANDARDS IN 2011

In January 2009, the AcSB published Section 1582, "Business Combinations," Section 1601, "Consolidated Financial Statements," and Section 1602, "Non-controlling Interests" which replace Section 1581, "Business Combinations," and Section 1600, "Consolidated Financial Statements." These sections require, for instance, that non-controlling interests be recognized as a separate component of shareholder equity rather than as a liability, which can no longer be deducted from net investment results due to their presentation in equity.

In accordance with the transitional provisions, these sections will be applied prospectively starting January 1, 2011, with the exception of presentation requirements affecting non-controlling interests, which must be applied retroactively. Adoption of these sections will have no material impact on the Combined Financial Statements, but will lead to the reclassification of non-controlling interests.

## EXTERNAL AUDIT

The Caisse's Financial Statements are prepared in accordance with Canadian generally accepted accounting principles, complying with the Act respecting the Caisse de dépôt et placement du Québec.

As required by law, the Caisse's co-auditors audited the institution's accounting records for fiscal year 2010 and issued their reports on the Caisse's financial statements. Overall, the co-auditors reported on 61 financial statements, namely the Caisse's Combined Financial Statements and those of the General Fund, 36 individual funds of the depositors (one of which ceased to be active during 2010) and 23 specialized portfolios (6 of which were dissolved in 2010). They issued an auditors' report without modification for each of these financial statements.

# Fair Value Measurement

Investment valuation is a process whereby a value is assigned to each investment of the Caisse in preparing its financial statements. The valuation of investments at fair value is performed periodically according to policies and processes specific to each type of investment. These procedures comply with the standards and practices of Canadian and international organizations, involving the use of stock market, valuator or independent expert valuations. The co-auditors review all major valuation files as part of their audit of year-end financial statements.

## ACCOUNTING PROVISIONS

According to Accounting Guideline AcG-18, "Investment Companies," of the CICA Handbook, the Caisse must determine the fair value of its investments based on the assumption that they are available for sale on the preparation date of its financial statements. This accounting guidance draws heavily on recent international developments in fair value measurement accounting standards. The purpose of these standards is to define a conceptual framework for all standards that require fair value measurement.

Under normal circumstances, the fair value (mark-to-market) rule is not a problem since all financial markets are active and investment values can be based on actual transactions involving comparable assets in various markets. However, when markets are disrupted (i.e. there are no purchases or sales), fair value must be determined by a financial model based on discounted cash flows (mark-to-model) whose parameters, namely financing and illiquidity premiums, are exposed to a certain level of subjectivity from firm to firm or valuator to valuator. The higher the premiums, the lower the fair value of the investments.

## IMPACT ON THE CAISSE'S INVESTMENTS

The Caisse believes that these standards provide a coherent framework, but must be applied with discretion. These highly restrictive standards ignore the fact that, given the very long investment horizon adopted by its major depositors, the Caisse has the resources and intent to hold certain investments until their optimal value is reached.

As a result, the fair value determined as at December 31, 2010, for illiquid market investments, such as real estate, private equity, infrastructure, commercial debt and commercial mortgages, reflects the overall volatility of financial markets, which may deviate from the economic value of long-term holdings.

## ESTABLISHING FAIR VALUE AT THE CAISSE

### Liquid investments

The fair value of liquid investments is based on major stock market quotes, dealer or other specialized agency ratings or inputs and recognized capital market valuation methods, such as discounting future cash flows at the current interest rate. Quarterly, certain portfolios, and, semi-annually, all portfolios of unlisted liquid products are valued by independent professionals. These products, which include bonds and over-the-counter derivatives, are valued on both a valuation model and input basis.

### Private equity and infrastructure

The fair value of private equity and infrastructure investments is determined semi-annually, at June 30 and December 31, unless significant circumstances require a change in value of an investment at another time during the year. The valuation is based on a policy adopted by the Caisse's Board of Directors. The policy draws on the industry's best practices. This enables managers to value their private equity investments before approval by the Private Equity group's management. Investments whose fair value exceeds a predetermined materiality threshold must be submitted to an independent valuation committee or an external independent valuator. The committee, which reports to the Caisse's Audit Committee, is composed of independent valuation professionals. The co-auditors attend the committee's meetings. The process is complemented internally by regular and timely valuations, as events occur.

**Real estate investments**

The fair value of real estate investments is determined semi-annually, at June 30 and December 31, unless significant circumstances require a one-time investment valuation adjustment. The valuation of the specialized Real Estate portfolio's investments is based on a policy adopted by the Caisse's Board of Directors. The policy draws on the industry's best practices. The fair value of the specialized Real Estate portfolio's assets is certified by external chartered valuers. The fair value of other real estate investments is largely determined by external managers. Internal managers determine the fair value of debt associated with real estate investments. In addition, the real estate subsidiaries' external auditors audit fair values in preparing audited financial statements.

The fair value of mortgage loans and securities is based on the discounted value of future contractual cash flows at the market interest rate. This is the rate that could be obtained for loans or securities with similar terms and maturities. In cases where the timing of cash flows cannot be estimated with reasonable reliability, fair value is either the fair value of any asset given as collateral, net of expected costs of realization and any amount legally owed to borrowers, or the security's relevant market price. The Caisse relies on an independent professional valuation or a subsidiary's externally audited financial statements.

Finally, for the specialized Real Estate and Real Estate Debt portfolios, the co-auditors rely on the work of external auditors and review valuation reports in auditing the Caisse's books and accounts.

**ABTNs**

Asset-backed term notes (ABTNs) are financial instruments with an average maturity of less than seven years. To provide an economic hedge to reduce the risk of loss inherent in ABTNs fair value changes and possible collateral calls, the Caisse uses financial derivatives such as interest rate and credit default swaps.

Before 2010, the Caisse determined the fair value of ABTNs by estimating the discounted value of cash flows. Since January 1, 2010, in connection with the implementation of the economic hedge, the Caisse changed its method for establishing the fair value of most ABTNs. To determine fair value, the Caisse relies on a database that contains the original contractual information underlying credit derivative transactions. The fair value of these notes and associated financial derivatives is based on valuation techniques for each underlying asset class. These valuation techniques are based as much as possible on observable market data such as rate spreads and interest rates, correlation factors and illiquidity premium, which is calculated from the difference between the bid and offer prices for similar financial instruments in the market. Finally, the fair value of the ABTNs as at December 31, 2010, was reviewed by an independent firm and its report was reviewed by the Caisse's external auditors.



# Combined financial statements

# Management's responsibility for combined financial reporting

Preparation and presentation of the combined financial statements of the Caisse de dépôt et placement du Québec (the "Caisse") are the responsibility of management. The combined financial statements were prepared in accordance with Canadian generally accepted accounting principles (GAAP). We ensure that the financial data in the Annual Report are consistent with those in the combined financial statements.

The combined financial statements include amounts based on management's best estimates and judgment, with due regard for their relative importance. Moreover, in the preparation of the financial data, management has made decisions regarding the information to be presented, has made estimates and has made assumptions that affect the information presented. Future results may differ considerably from our current estimates, because of changes in the financial markets or other events that may have an impact on the fair value of the investments established as at December 31, 2010.

In our responsibility for the reliability of financial information, we use a sophisticated internal control mechanism applied systematically on all levels of the organization. This mechanism consists of organizational and operational controls, financial information disclosure controls and procedures, and internal control over financial information. The Caisse's internal control mechanism is based, among other things, on a clear definition of responsibilities, effective allocation of duties, delegation of powers, competent resources, appropriate procedures, information systems, tools and practices, relevant and reliable information whose adequacy enables all employees to fulfill their responsibilities, control, compliance and integrated risk management measures that are proportional to the issues specific to each process and designed to reduce risks likely to affect achievement of the Caisse's objects, and oversight of compliance with an extensive body of internal policies.

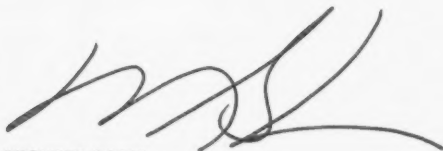
This control mechanism makes it possible to ensure that appropriate internal controls are in place as regards operations, assets and records. Moreover, the Caisse's internal audit group reviews the internal controls on a regular basis. These controls and audits are designed to provide reasonable assurance regarding the reliability of the accounting records used to prepare the combined financial statements and to ensure that assets are not used or disposed of in any unauthorized manner, that liabilities are recorded, and that we meet all the legal requirements to which the Caisse is subject, including the Act respecting the Caisse de dépôt et placement du Québec.

Each year, we certify that the design of the internal control regarding financial information is sufficient and that the design and functioning of the financial information disclosure controls and procedures are effective. We report any significant irregularity to the Audit Committee of the Board of Directors of the Caisse, as necessary.

The Auditor General of Québec and Ernst & Young LLP (the "co-auditors") have audited the combined financial statements of the Caisse, and their report covers the nature and scope of the audit and expresses their opinion. The co-auditors have unrestricted access to the Audit Committee to discuss any matter relating to their audit.

The Board of Directors and its committees supervise the manner in which management fulfills its responsibility for the establishment and presentation of financial information, maintenance of appropriate internal controls, compliance with the requirements of laws and regulations, management of and control over the main risks and evaluation of major transactions. Moreover, it approves the combined financial statements and the Annual Report.

The Board of Directors has approved the combined financial statements as at December 31, 2010. It is assisted in its responsibilities by the Audit Committee, of which all members are outside directors. This Committee meets with management and the co-auditors, examines the combined financial statements and recommends their approval to the Board of Directors.



**MICHAEL SABIA**

President and Chief Executive Officer  
and Acting Chief Financial Officer

Montréal, February 22, 2011

# Independent auditors report

To the National Assembly

## Report on the combined financial statements

We have audited the combined financial statements of the Caisse de dépôt et placement du Québec, which comprise the combined statement of net assets as at December 31, 2010, and the combined statement of income and changes in net assets for the year then ended, and a summary of significant accounting policies and other explanatory information.

### Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these combined financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of combined financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors responsibility

Our responsibility is to express an opinion on the combined financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risks assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the combined financial statements in order to design audit procedures that are appropriate to the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the combined financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the combined financial statements present fairly, in all material respects, the financial position of the Caisse de dépôt et placement du Québec as at December 31, 2010, as well as the results of its operations and the changes in its net assets for the year then ended, in accordance with Canadian generally accepted accounting principles.

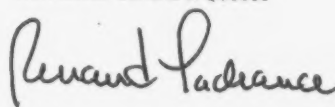
### Other matter

The combined financial statements of the Caisse de dépôt et placement du Québec for the year ended December 31, 2009, were audited by the Auditor General of Québec, who expressed an unmodified opinion on those statements on February 15, 2010.

## Report on other legal or regulatory requirements

As required by the *Auditor General Act* (R.S.Q., chapter V-5.01), we report that, in our opinion, the accounting principles have been applied on a basis consistent with that of the preceding year.

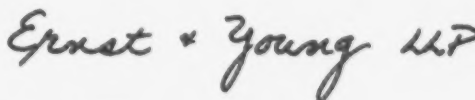
The Auditor General of Québec

  
FCA auditor

Renaud Lachance, FCA auditor

Montréal, February 22, 2011

Ernst & Young LLP



CA auditor permit no. 15859

Montréal, February 22, 2011

# Combined statement of net assets

as at December 31

(in millions of dollars)

	2010	2009
<b>Assets</b>		
Investments at fair value (notes 4A, B and E)	178,376	167,575
Advances to depositors	789	371
Investment income, accrued and receivable	933	1,042
Transactions being settled	177	70
Other assets	2,922	1,598
	<b>183,197</b>	<b>170,656</b>
<b>Liabilities</b>		
Liabilities related to investments (notes 4C and E)	28,055	34,830
Transactions being settled	563	1,478
Other liabilities	1,062	1,200
Non-controlling interests (note 4D)	1,775	1,560
	<b>31,455</b>	<b>39,068</b>
<b>Depositors' net holdings (note 5)</b>	<b>151,742</b>	<b>131,588</b>

Derivative financial instruments (note 10)

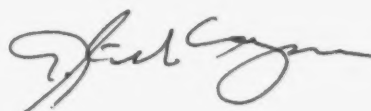
Commitments and contingencies (note 12)

The accompanying notes are an integral part of the combined financial statements.

For the Board of Directors,



MICHAEL SABIA



A. MICHEL LAVIGNE

# Combined statement of income and changes in net assets

For years ended December 31

(in millions of dollars)	2010	2009
Investment income ( <i>note 6A</i> )	4,850	4,893
Less:		
Operating expenses ( <i>note 7</i> )	257	250
Repositioning expenses and write-offs of intangible assets ( <i>note 8</i> )	34	—
Net investment income	4,559	4,643
Gains on the sale of investments ( <i>note 6D</i> )	1,582	4,514
<b>Total realized income</b>	<b>6,141</b>	<b>9,157</b>
Unrealized increase in value of investments and liabilities related to investments ( <i>note 6E</i> )	11,590	2,596
<b>Net investment results</b>	<b>17,731</b>	<b>11,752</b>
Depositors net deposits (withdrawals)	2,423	(252)
<b>Increase in combined net assets</b>	<b>20,154</b>	<b>11,500</b>
<b>Combined net assets, beginning of year</b>	<b>131,588</b>	<b>120,088</b>
<b>Combined net assets, end of year</b>	<b>151,742</b>	<b>131,588</b>

The accompanying notes are an integral part of the combined financial statements.

# Combined funds notes to financial statements

As at December 31, 2010

## 01

### CONSTITUTION AND OPERATIONS

The Caisse de dépôt et placement du Québec ("Caisse"), a legal person established in the public interest within the meaning of the *Civil Code*, is governed by the Act respecting the *Caisse de dépôt et placement du Québec (R.S.Q., chapter C-2)* ("Act"). It receives all funds, the deposit of which is provided under the Act. Pursuant to the federal and provincial income tax acts, the Caisse is not subject to income taxes.

### GENERAL FUND (CONSOLIDATED STATEMENTS)

The General Fund comprises all treasury operations (management of demand and term deposits, and corporate financing of the Caisse).

On January 1, 2010, the assets, liabilities and unrealized decrease in value pertaining to ABTNs were transferred, respectively, from the specialized Bonds portfolio (760) and from the General Fund to the new specialized ABTNs portfolio (772). In addition, the financial instrument between the specialized Bonds portfolio (760) and the General Fund which was used to allocate the net investment results of the ABTNs to the individual funds was not renewed.

Since September 1, 2010, the General Fund has held the participation units of specialized portfolios which were financed by term deposits of a depositor. The net investment results resulting from such holding are redistributed on a monthly basis to the holder of the corresponding term deposits.

### INDIVIDUAL FUNDS

The individual funds are comprised of diversified investments, and each fund has only one depositor that exclusively makes participation deposits therein. The individual funds are for the use of the following depositors:

- Fund 300:** Fonds du Régime de rentes du Québec administered by the Régie des rentes du Québec;
- Fund 301:** Government and Public Employees Retirement Plan administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 302:** Pension Plan for Management administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 303:** Individual plans administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 305:** Pension Plan for Elected Municipal Officers administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 306:** Régime complémentaire de rentes des techniciens ambulanciers/paramédics et des services préhospitaliers d'urgence administered by Aon Conseil;
- Fund 307:** Fonds d'assurance automobile du Québec administered by the Société de l'assurance automobile du Québec;
- Fund 311:** Supplemental Pension Plan for employees of the Québec construction industry – general account – administered by the Commission de la construction du Québec;
- Fund 312:** Supplemental Pension Plan for employees of the Québec construction industry – retirees account – administered by the Commission de la construction du Québec;
- Fund 313:** Supplemental Pension Plan for employees of the Québec construction industry – supplementary account – administered by the Commission de la construction du Québec;
- Fund 314:** Fonds d'assurance-dépôts administered by the Autorité des marchés financiers;
- Fund 315:** Fonds d'assurance-prêts agricoles et forestiers administered by La Financière agricole du Québec;
- Fund 316:** Fonds d'amortissement du régime de retraite – RREGOP administered by the ministère des Finances, Government of Québec;
- Fund 317:** Fonds d'amortissement du régime de retraite – RRPE administered by the ministère des Finances, Government of Québec;
- Fund 318:** Fonds d'amortissement des autres régimes de retraite administered by the ministère des Finances, Government of Québec;
- Fund 326:** Fonds d'assurance-récolte administered by La Financière agricole du Québec;
- Fund 327:** Fédération des producteurs de bovins du Québec (inactive since September 1, 2010);
- Fund 328:** Régime de rentes de survivants administered by the Conseil du trésor, Government of Québec;
- Fund 329:** Fonds d'assurance-garantie administered by the Régie des marchés agricoles et alimentaires du Québec;

## CONSTITUTION AND OPERATIONS (cont.)

- Fund 330:** Fonds de la santé et de la sécurité du travail administered by the Commission de la santé et de la sécurité du travail;
- Fund 332:** Fonds des cautionnements des agents de voyages – cautionnements individuels – administered by the Office de la protection du consommateur;
- Fund 333:** Fonds d'indemnisation des clients des agents de voyages administered by the Office de la protection du consommateur;
- Fund 341:** Fonds pour l'éducation et la saine gouvernance – Fonds de trésorerie – administered by the Autorité des marchés financiers;
- Fund 342:** Régime de retraite de l'Université du Québec administered by the Comité de retraite du Régime de retraite de l'Université du Québec;
- Fund 343:** Fonds d'assurance parentale administered by the Conseil de gestion de l'assurance parentale;
- Fund 347:** Régime de retraite du personnel des CPE et des garderies privées conventionnées du Québec administered by Aon Conseil;
- Fund 348:** Régime complémentaire de retraite des employés syndiqués de la Commission de la construction du Québec administered by the Comité de retraite du Régime complémentaire de retraite des employés syndiqués de la CCQ;
- Fund 351:** Fonds des générations administered by the ministère des Finances, Government of Québec;
- Fund 353:** Régime de retraite des membres de la Sûreté du Québec – caisse participants – administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 354:** Régime de retraite des membres de la Sûreté du Québec – caisse employeurs – administered by the Commission administrative des régimes de retraite et d'assurances (created January 1, 2010);
- Fund 361:** Régime de rentes pour le personnel non enseignant de la Commission des écoles catholiques de Montréal administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 362:** Régime de retraite pour certains employés de la Commission scolaire de la Capitale administered by the Commission administrative des régimes de retraite et d'assurances;
- Fund 363:** Régime de retraite des employés de la Ville de Laval administered by the Comité du Régime de retraite des employés de la Ville de Laval;
- Fund 368:** Fonds pour l'éducation et la saine gouvernance – Fonds capitalisé – administered by the Autorité des marchés financiers;
- Fund 369:** Fonds des congés de maladie accumulés administered by the ministère des Finances, Government of Québec; and
- Fund 373:** Régime de retraite des employés en fonction au Centre hospitalier Côte-des-Neiges administered by the Commission administrative des régimes de retraite et d'assurances (created July 1, 2010).

## SPECIALIZED PORTFOLIOS

The specialized portfolios are pooled funds for participation deposits of the various funds. In 2010, as a result of the new specialized portfolio offer available to depositors, the Caisse created or dissolved certain specialized portfolios. The specialized portfolios are the following:

- Real Estate (710) (consolidated statements)
- Canadian Equity (720)
- Foreign Equity – Hedged (730) (dissolved April 1, 2010)<sup>1</sup>
- EAFE Equity (730) (created April 1, 2010)
- U.S. Equity – Hedged (731) (dissolved April 1, 2010)<sup>1</sup>
- U.S. Equity (731) (created April 1, 2010)
- Emerging Markets Equity (732)
- Foreign Equity – Unhedged (733) (dissolved April 1, 2010)<sup>1</sup>
- U.S. Equity – Unhedged (734) (dissolved April 1, 2010)<sup>1</sup>
- Global Equity (735) (created April 1, 2010)
- Short-term Investments (740)
- Real Estate Debt (750) (consolidated statements)
- Bonds (760)
- Québec International (761)
- Real Return Bonds (762)
- Commodity Financial Instruments (763) (dissolved December 1, 2010)<sup>2</sup>
- Long-term Bonds (764)
- Hedge Funds (770) (consolidated statements)
- Asset Allocation (771)
- ABTNs (772) (created January 1, 2010)
- Private Equity (780) (consolidated statements)
- Investments and Infrastructures (781) (consolidated statements) (dissolved July 1, 2010)<sup>3</sup>
- Infrastructure (782) (consolidated statements) (created July 1, 2010)

1. The investment operations of these portfolios were transferred on April 1, 2010, to the new specialized Global Equity, U.S. Equity and EAFE Equity portfolios.

2. The investment operations of this portfolio were transferred on December 1, 2010, to the specialized Asset Allocation portfolio.

3. The investment operations of this portfolio were transferred on July 1, 2010, to the new specialized Infrastructure portfolio and to other specialized portfolios.

## 02

### ACCOUNTING POLICIES

The preparation of the combined financial statements of the Caisse in accordance with Canadian generally accepted accounting principles requires that management make estimates and assumptions, which have an impact on the accounting of assets and liabilities, the presentation of contingent assets and liabilities at the date of the financial statements and the accounting of revenues and expenses during the financial year covered by the combined financial statements. Actual results may differ from such estimates.

The Caisse is considered an investment company pursuant to the accounting guideline "Investment Companies" (AcG-18) of the Handbook of the Canadian Institute of Chartered Accountants (CICA). Accordingly, all the investments of the Caisse are presented at fair value.

A statement of cash flows is not presented, as it would provide no further useful information for the comprehension of cash flows during the year.

#### A) COMBINED FINANCIAL STATEMENTS

The combined financial statements comprise the accounts of the subsidiaries controlled by the Caisse, along with those of the General Fund, the individual funds and the specialized portfolios. The Caisse consolidates the investments in the subsidiaries when they do not meet certain criteria envisaged by the AcG-18. The financial statements of each fund and each portfolio are audited by the joint auditors of the Caisse. All transactions and balances between related parties have been eliminated. Summary financial statements for the specialized portfolios are in the section Supplementary Information.

#### B) INVESTMENTS AND RELATED OPERATIONS

Investments and related assets and liabilities are accounted for at fair value, which is the estimated exchange value that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act, established at year-end.

Transaction costs that are directly attributable to the acquisition and sale of investments are included in income and applied against gains and losses on the sale of investments. Transaction costs include commissions, stock exchange fees and professional and legal fees related to investment operations.

##### FIXED-INCOME SECURITIES

Fixed-income securities comprise short-term investments, bonds, asset-backed term notes ("ABTNs"), mortgages, commercial paper payable, term notes, mortgage loans payable and other loans payable. Acquisitions and sales of fixed-income securities are recorded at the transaction date, except for mortgages, which are recorded at the settlement date.

##### i) VALUATION METHOD

The fair value of short-term investments and bonds is determined by the market price, when such a value is available. When a market price is not available, the fair value of the securities is established according to valuation methods used in capital markets, such as discounting of future cash flows, or according to similar transactions on an arm's-length basis. These valuations are supported by observable or non-observable input data, such as interest rate yield curves, credit spreads or discount rates. The valuation method for ABTNs is discussed in note 4B.

The fair value of mortgages is determined from the present value of future contractual cash flows at the market interest rate. The rate is that which could be obtained for loans or securities with similar conditions and maturities. Where the timing of future cash flows cannot be estimated in a reasonably reliable fashion, the fair value corresponds either to the fair value of any collateral, less expected realization costs and any amount legally owed to borrowers, or to the observable market price for the mortgages.

The fair value of most fixed-income securities is reviewed biannually by independent external firms.

The valuation methods are applied on a consistent basis, with the exception of ABTNs (refer to note 4B).

##### ii) INVESTMENT INCOME AND GAINS AND LOSSES ON THE SALE OF INVESTMENTS

Investment income from fixed-income securities includes amortization of the premium or the discount, which makes it possible to maintain a constant effective yield until maturity. Income from mortgages is reduced by operation expenses and financial costs of commercial mortgage-backed securities (CMBS) and is recorded under the item Investment income - Fixed-income securities.

Gains and losses on the sale of investments represent the difference between the amortized cost and the net realizable value on the sale of investments. The amortized cost corresponds to the acquisition cost adjusted to reflect amortization of the premium or the discount.

**ACCOUNTING POLICIES (cont.)****VARIABLE-INCOME SECURITIES**

Variable-income securities comprise equities and convertible securities as well as real estate holdings. Acquisitions and sales of equities and convertible securities are recorded at the transaction date, whereas acquisitions and sales of real estate holdings are recorded at the settlement date.

**i) VALUATION METHOD**

The fair value of listed equities and convertible securities is determined from prices on major stock exchanges. For unlisted equities and convertible securities, prices are provided by recognized financial institutions or valuations are made according to commonly used valuation methods, such as the earnings multiples of comparable listed companies, discounting of cash flows, or on the basis of similar transactions on an arm's-length basis. These valuations are supported by observable or non-observable input data, such as EBITDA multiples, price/earnings multiples, price/book value ratios, discount rates and future cash flows. The valuations of unlisted equities and convertible securities are reviewed biannually by a valuation committee made up of independent experts or by independent external firms.

The fair value of investment funds is determined from the fair value provided by the general partner or the administrator, in accordance with commonly used valuation methods.

Real estate holdings include partial or full ownership of income properties through interests in a company or a partnership. The fair value of income properties included in real estate holdings is determined and certified biannually by external, recognized and independent chartered real estate appraisers. The valuation techniques used for income properties are based mainly on three recognized methodologies: discounting of cash flows at the market rate, comparison with recent similar market transactions and capitalization of earnings. These valuations are supported by observable or non-observable input data, such as leases, operating expenses, rates of return and discount rates. The valuations are established in accordance with commonly used professional valuation standards.

The valuation methods are applied on a consistent basis.

**ii) INVESTMENT INCOME AND GAINS AND LOSSES ON THE SALE OF INVESTMENTS**

Dividend income is recognized on the ex-dividend date. Income from real estate holdings is reduced by operating expenses, operation expenses and loan financial expenses, and is recorded under the item Investment income – Variable-income securities.

Gains and losses on the sale of investments represent the difference between the cost and the net realizable value on the sale of investments. The cost of investments corresponds to the acquisition cost, with the exception of the cost of investments in joint ventures, which are recorded on an equity basis.

**DERIVATIVE FINANCIAL INSTRUMENTS**

In managing its investments, the Caisse conducts transactions involving various derivative financial instruments to manage the risks associated with exchange rate, interest rate and market fluctuations.

Derivative financial instruments whose fair value is favourable are recorded under the item Investments at fair value, whereas those whose fair value is unfavourable are recorded under Liabilities related to investments.

**i) VALUATION METHOD**

For over-the-counter derivative financial instruments, prices are provided by recognized financial institutions or valuations are made from similar transactions on an arm's-length basis or with recognized, commonly used models. The models used include discounting of future cash flows at the current rate of return and the Black-Scholes model. These models require the use of assumptions regarding the amount and timing of future cash flows and the current rate of return. The assumptions are prepared with observable and non-observable input data, such as interest rate yield curves, credit spreads and foreign exchange rates as well as the volatility and correlation of equity prices, commodity prices and interest rates. The fair value estimates of most over-the-counter derivative financial instruments are reviewed biannually by independent external firms. If necessary, the fair value of listed derivative financial instruments is determined from prices on major stock exchanges.

The valuation methods are applied on a consistent basis.

**ii) INVESTMENT INCOME AND GAINS AND LOSSES ON THE SALE OF INVESTMENTS**

Investment income from derivative financial instruments is included with income from fixed-income and variable-income securities, whereas gains and losses pertaining to derivative financial instruments are included with gains and losses on the sale of investments depending on the underlying investments.

**ACCOUNTING POLICIES (cont.)****SECURITIES ACQUIRED UNDER REVERSE REPURCHASE AGREEMENTS**

The Caisse conducts securities-borrowing operations involving short-term investments and bonds to cover short sales or to generate additional income from securities-borrowing operations. These securities-borrowing operations are recorded in Securities acquired under reverse repurchase agreements under Investments at fair value. Interest earned on reverse repurchase agreements is recorded as interest income under the item Investment income – Fixed-income securities.

**SECURITIES SOLD UNDER REPURCHASE AGREEMENTS**

The Caisse conducts securities-lending operations involving short-term investments and bonds to generate cash flow liquidity or additional income. These securities-lending operations are recorded in Securities sold under repurchase agreements under Liabilities related to investments. Interest paid on repurchase agreements is applied against Investment income – Fixed-income securities.

**SHORT SELLING OF SECURITIES**

Short selling of securities represents the commitment by the Caisse to purchase securities from third parties to cover its positions. Interest expenses related to commitments involving short selling of short-term investments and bonds are recorded under Investment income – Fixed-income securities, whereas costs related to commitments involving short selling of equities are recorded under Investment income – Variable-income securities.

Gains and losses on commitments related to short selling of short-term investments and bonds are recorded in Gains (losses) on the sale of investments – Fixed-income securities, whereas those related to short selling of equities are recorded in Gains (losses) on the sale investments – Variable-income securities.

**HIERARCHY OF FAIR VALUE**

The Caisse's financial instruments are classified according to the following hierarchy:

- Level 1: Calculation of the fair value of the instrument is based on prices (not adjusted) quoted on active markets for identical assets or liabilities.
- Level 2: Calculation of the fair value of the instrument is based on data other than the quoted prices contemplated in level 1, which are observable directly (in the form of prices) or indirectly (determined from prices). This level includes instruments whose valuation is based on prices quoted on markets that are not active for identical instruments and instruments whose valuation is based on prices observed for similar instruments as well as valuation techniques based on assumptions that take into account observable market data.
- Level 3: Calculation of the fair value of the instrument uses data that are not based on observable market data (non-observable data). This level includes instruments whose valuation is based on prices observed for similar instruments, adjusted to reflect the differences between the instruments being valued and the available market data. This level also includes instruments whose valuation is based on valuation techniques using assumptions that take into account market data that are observable but are adjusted significantly to reflect the specific characteristics of the instrument being valued.

The classification of financial instruments in the levels of the hierarchy is established at the time of the initial valuation of the instrument and reviewed on each subsequent valuation date. Transfers between the hierarchical levels are measured at fair value at the start of each quarter.

Quantitative information on the hierarchy of fair value is given in note 4E.

**C) ADMINISTERED PROPERTY AND PROPERTIES UNDER MANAGEMENT**

The Caisse and its subsidiaries administer and manage properties entrusted to them by clients and on their behalf. These properties are not included in the Combined statement of net assets of the Caisse. The Caisse and its subsidiaries receive fees in return for such portfolio management services and administrative services, which include the administration of real estate properties and transferred mortgages.

**D) FOREIGN CURRENCY TRANSLATION**

The fair value of investments as well as any other assets and liabilities denominated in foreign currencies is translated into Canadian dollars at the rate of exchange prevailing at year-end.

**ACCOUNTING POLICIES (cont.)**

To present in the Combined statement of income and changes in net assets the amount of gains and losses on the sale of investments or unrealized gains (losses), the cost of investments in equities and that of real estate holdings from integrated foreign operations and the amortized cost of investments in short-term investments, bonds and mortgages are translated at the rate of exchange prevailing on the acquisition date. The cost of investments from self-sustaining foreign operations is translated at the rate of exchange prevailing at year-end.

Income is translated at the rate of exchange prevailing on the transaction date, with the exception of income from the specialized Real Estate portfolio, which is translated at the average rate for the year.

**E) TRANSFERS OF RECEIVABLES**

The Caisse occasionally securitizes or transfers mortgages by selling them directly to companies or through a conduit, which subsequently issues securities to investors.

Such transactions are recorded as sales where the Caisse is deemed to have surrendered control over such assets and to have received consideration other than beneficial interests in the transferred assets, in accordance with Accounting Guideline AcG-12 "Transfers of Receivables" in the CICA Handbook. At the time of securitization or transfer, no beneficial interest in the mortgages is retained. Any gains or losses deriving from such transactions are recorded under Gains (losses) on the sale of investments – Mortgages and Bonds.

Companies under common control usually continue to service transferred loans. Since servicing fees are marked-based, no servicing assets or liabilities are recorded at the date of transfer.

**F) OPERATING EXPENSES**

Operating expenses represent all expenses related to portfolio management and administration, with the exception of those related to external management. Operating expenses are recorded under a separate line item in the Combined statement of income and changes in net assets. Expenses related to management of the specialized Real Estate and Real Estate Debt portfolios are included in operating expenses. Expenses related to the real estate and real estate debt subsidiaries are deducted from real estate holdings investment income and mortgages investment income, respectively.

**G) EXTERNAL MANAGEMENT FEES**

External management fees represent amounts paid to external financial institutions, principally institutional fund managers active on international stock markets, for the management of Caisse funds on behalf of the Caisse. Basic external management fees and management fees related to the performance of external managers are deducted from Investment income and Gains (losses) on the sale of investments, respectively.

**03****FUTURE ACCOUNTING CHANGES**

Canadian publicly accountable enterprises are obliged to apply International Financial Reporting Standards (IFRS) to replace Canadian generally accepted accounting principles (GAAP), starting January 1, 2011. The Accounting Standards Board (AcSB) decided in 2010, however, to allow deferral of the date of the first application of IFRS to investment companies that apply AcG-18 of the CICA Handbook. Moreover, the AcSB decided on January 12, 2011 to extend by one additional year the deferral of the mandatory IFRS changeover for these entities. The Caisse will therefore prepare its combined financial statements in accordance with IFRS starting January 1, 2013.

In January 2009, the AcSB published section 1582, "Business Combinations," section 1601, "Consolidated Financial Statements," and section 1602, "Non-controlling Interests," which replace section 1581 "Business Combinations," and section 1600, "Consolidated Financial Statements." These sections require, among other things, that non-controlling interests be presented as a separate line item within equity rather than as a liability, and that they no longer be deducted from net investment results as a result of their presentation in equity.

In accordance with the transitional provisions, these sections will be applied prospectively starting January 1, 2011, with the exception of the presentation requirements affecting non-controlling interests, which must be applied retroactively. Adoption of these sections will have no material impact on the combined financial statements, but will give rise to reclassification of non-controlling interests.

## 04

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

## A) INVESTMENTS

(in millions of dollars)

	2010		2009	
	Fair value	Cost	Fair value	Cost
<b>Fixed-income securities</b>				
<b>Short-term investments</b>				
Canadian	2,357	2,370	4,625	4,684
Foreign	1,614	1,802	2,376	2,860
	<b>3,971</b>	<b>4,172</b>	<b>7,001</b>	<b>7,544</b>
<b>Bonds</b>				
<i>Issued or guaranteed by:</i>				
Government of Canada	21,637	21,149	21,652	21,600
Province of Québec	8,801	8,305	7,859	7,380
Other Canadian provinces	1,658	1,586	3,158	3,154
Municipalities and other				
Canadian agencies	1,280	1,247	1,279	1,276
Canadian government corporations	11,998	11,322	10,482	9,883
U.S. government	1,379	1,641	510	741
Other foreign governments	17	17	346	339
Mortgage securities				
Canadian	213	230	245	258
Foreign	68	314	233	2,408
Canadian corporations	8,831	8,906	9,830	10,257
Foreign corporations	1,678	2,197	2,269	3,174
Inflation-indexed securities				
Canadian	975	895	667	618
Hedge funds	-	-	72	99
	<b>58,535</b>	<b>57,809</b>	<b>58,602</b>	<b>61,187</b>
<b>ABTNs (note 4B)</b>	<b>7,850</b>	<b>11,910</b>	<b>7,249</b>	<b>12,351</b>
<b>Mortgages</b>				
Canadian	5,886	5,780	5,944	6,104
Foreign	1,667	2,932	2,871	5,427
	<b>7,553</b>	<b>8,712</b>	<b>8,815</b>	<b>11,531</b>
<b>Total fixed-income securities</b>	<b>77,909</b>	<b>82,603</b>	<b>81,667</b>	<b>92,613</b>
<b>Variable-income securities</b>				
<b>Equities and convertible securities</b>				
Canadian	17,180	14,640	14,449	14,498
U.S.	17,379	20,230	14,427	19,189
Foreign and emerging markets	26,398	25,496	19,693	19,794
Hedge funds	2,964	3,002	3,615	3,689
	<b>63,921</b>	<b>63,368</b>	<b>52,184</b>	<b>57,170</b>
<b>Real estate holdings</b>				
Canadian	12,880	10,482	10,930	9,279
Foreign	8,610	9,816	9,012	10,578
	<b>21,490</b>	<b>20,298</b>	<b>19,942</b>	<b>19,857</b>
<b>Total variable-income securities</b>	<b>85,411</b>	<b>83,666</b>	<b>72,126</b>	<b>77,027</b>

**INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)**

(in millions of dollars)		2010		2009	
	Fair value	Cost	Fair value	Cost	
<b>Amounts receivable with respect to investments</b>					
Securities acquired under reverse repurchase agreements					
Canadian	8,761	8,762	6,171	6,171	
Foreign	1,007	1,017	1,928	1,963	
Amount pertaining to derivative financial instruments					
Canadian	2,132	1,157	1,106	21	
Foreign	3,156	120	4,577	896	
	15,056	11,056	13,782	9,051	
<b>Total investments</b>	<b>178,376</b>	<b>177,325</b>	<b>167,575</b>	<b>178,691</b>	

As at December 31, the item Investments – Real estate holdings includes, among other things, investments in joint ventures recorded at fair value. The details of these investments are as follows:

(in millions of dollars)		2010	2009
<b>Investments in joint ventures</b>		<b>8,156</b>	<b>8,319</b>
Real estate holdings		12,745	13,601
Mortgages		2	2
Short-term investments		6	2
Investment income, accrued and receivable		78	13
Other assets		388	505
		13,219	14,123
Mortgage loans payable		4,400	5,088
Other loans payable		36	64
Derivative financial instruments		2	–
Other liabilities		569	596
Non-controlling interests		56	56
		5,063	5,804

**B) ABTNs AND RELATED FINANCIAL INSTRUMENTS**

As at December 31, 2010, the Caisse held asset-backed term notes ("ABTNs"), most of which were issued on January 21, 2009, under the restructuring agreement of the Pan-Canadian Investors Committee. The assets that were exchanged at that time were investments in the Canadian asset-backed commercial paper market. The notes are held through structures that take the form of trusts, which are called master asset vehicles, or "MAVs."

The ABTNs constitute debt backed by a variety of financial instruments. The underlying instruments are essentially credit default swaps for MAV 1 and MAV 2, while MAV 3 contains traditional assets, such as residential and commercial mortgage debt.

The Caisse uses derivative financial instruments, such as interest rate swaps and credit default swaps, to obtain economic hedge in order to reduce the risk of loss inherent in a fluctuation of the fair value of the ABTNs as well as eventual collateral calls. The credit default swaps were financed by the counterparty concerned. Repayment of this debt is related to cash flows from the repayment of certain investments held by MAV 1 and the related derivative financial instruments.

**INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)**

The ABTNs as well as other related financial instruments consist of the following as at December 31:

(in millions of dollars)						
	2010			2009		
	Fair value	Unrealized increase (decrease) in value	Cost	Fair value	Unrealized increase (decrease) in value	Cost
<b>Investments</b>						
MAV 1						
Class A-1	4,045	(480)	4,525	4,071	(476)	4,547
Class A-2	3,037	(788)	3,825	2,428	(1,397)	3,825
Class B	-	(652)	652	-	(652)	652
Class C	-	(279)	279	-	(279)	279
Notes for high-risk assets	44	(286)	330	-	(597)	597
Other notes	286	(22)	308	282	(26)	308
	7,412	(2,507)	9,919	6,781	(3,427)	10,208
MAV 2						
Class A-1	87	4	83	101	18	83
Class A-2	25	(2)	27	17	(10)	27
Class B	3	(2)	5	-	(5)	5
Class C	1	(3)	4	-	(4)	4
	116	(3)	119	118	(1)	119
MAV 3						
Notes for traditional assets	276	(112)	388	478	(59)	537
Notes for high-risk assets	4	(63)	67	-	(70)	70
	280	(175)	455	478	(129)	607
Funding facilities	(449)	(449)	-	(589)	(589)	-
Subtotal	7,359	(3,134)	10,493	6,788	(4,146)	10,934
ABTNs excluded from the restructuring agreement	491	(926)	1,417	461	(956)	1,417
Total ABTNs	7,850	(4,060)	11,910	7,249	(5,102)	12,351
Amount pertaining to derivative financial instruments <sup>1</sup>	1,092	(48)	1,140	-	-	-
Total investments	8,942	(4,108)	13,050	7,249	(5,102)	12,351
<b>Liabilities related to investments</b>						
Other loans payable <sup>1</sup>	1,504	(8)	1,512	171	-	171
Amount pertaining to derivative financial instruments <sup>1</sup>	24	24	-	20	20	-
	7,414	(4,124)	11,538	7,058	(5,122)	12,180

1. Included under the items in notes 4A and 4C.

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

## COMMITMENTS RELATED TO ABTNs

The following table summarizes commitments related to ABTNs as at December 31:

(in millions of dollars)	Maturity	2010	2009
		Amount of commitments	
MAV 1 MFF	July 2017	6,167	6,167
MAV 1 and MAV 2 SFF	—	—	300
Total		6,167	6,467

As part of the restructuring plan, the Caisse has provided the following funding facilities:

- *Margin funding facility ("MFF")*: The Caisse's share of this credit commitment of \$5,767 million, intended to cover possible collateral calls, has the same rank as that of other participants and matures in July 2017 or at an earlier date if all the credit default swap transactions are settled beforehand. Under a separate agreement, the Caisse has agreed to take an interest of \$400 million in the MFF commitments of a MAV 1 participant. As at December 31, 2010, the Caisse had not taken part in any collateral calls.
- *Senior funding facility ("SFF")*: In the event that the MAV 1 MFF and the equivalent MAV 2 facility prove insufficient to meet the collateral calls of the vehicle in question, an SFF has been put in place to provide access to additional liquidity. These commitments matured in July 2010.

## ESTABLISHMENT OF FAIR VALUE

Before 2010, the Caisse established the fair value of ABTNs by estimating the present value of cash flows. Since January 1, 2010, in line with setting in place the economic hedge, the Caisse has modified its valuation method for the fair value of MAV 1 ABTNs, certain ABTNs excluded from the restructuring agreement and MFF.

For MAV 1 ABTNs, certain ABTNs excluded from the restructuring agreement and credit default swaps used as economic hedging instruments, the Caisse now uses a database containing the original contractual information underlying the transactions involving credit derivative financial instruments. The fair value of these notes as well as that of the related derivative financial instruments is established with valuation techniques specific to each class of underlying asset. These valuation techniques are based as much as possible on observable market data, such as credit spreads and interest rates, correlation factors and an illiquidity premium, which is calculated from the spread between the bid and ask prices of similar financial instruments traded in the market.

For the other ABTNs, the Caisse establishes fair values using a valuation technique based on a financial model whose assumptions use as much as possible observable market data, such as interest rates and credit quality. The fair value of the securities is established by estimating the present value of cash flows according to various default and loss-of-credit scenarios for all the underlying assets for each note, maturities corresponding to those of the underlying assets and interest rates reflecting the cash flows available within the vehicles, and takes into account the leverage rates of the various structures as well as subordination of the restructured notes, as required. Once adjusted to take into account the incidence of the credit risk of the underlying assets, the cash flows expected from the securities are discounted at a risk-free rate, plus an illiquidity premium.

Since 2010, the fair value of the MFF is established by applying a valuation technique using a discount rate based on the CDX.IG index tranches, plus a financing premium.

The estimated fair value of the ABTNs is not likely to be indicative of their definitive value or future fair value. Although management believes that its valuation technique is appropriate in the circumstances, the use of reasonably possible alternative assumptions could have a material impact on the fair value of the ABTNs in the years to come. Accordingly, resolution of these uncertainties could mean that the definitive value of the investments in subsequent periods differs considerably from management's current best estimates.

A downward variation of 3.45% of credit spreads would involve an increase in the fair value of the ABTNs net of economic hedge of \$43 million. An upward variation of 3.45%, however, would result in a decrease of \$45 million in the net fair value.

When the financial statements were prepared, there was still no active market for ABTNs.

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

## C) LIABILITIES RELATED TO INVESTMENTS

(in millions of dollars)				
	2010		2009	
	Fair value	Cost	Fair value	Cost
Securities sold under repurchase agreements				
Canadian	338	338	9,115	9,113
Foreign	629	632	1,223	1,458
Commercial paper payable				
Canadian	1,017	1,017	1,288	1,288
Term notes				
Canadian	2,044	1,998	—	—
Foreign	6,051	6,287	5,075	5,345
Short selling of securities				
Canadian	6,267	5,444	4,593	4,145
Foreign	2,498	2,543	2,980	2,616
Mortgage loans payable				
Canadian	679	635	855	833
Foreign	2,156	2,208	3,351	3,513
Other loans payable				
Canadian	1,710	1,816	833	836
Foreign	1,283	1,222	1,162	1,210
Amount pertaining to derivative financial instruments				
Canadian	527	57	442	53
Foreign	2,856	301	3,913	1,214
	28,055	24,498	34,830	31,624

## D) NON-CONTROLLING INTERESTS

(in millions of dollars)				
	2010		2009	
	Fair value	Cost	Fair value	Cost
Canadian	1,480	1,380	1,208	1,252
Foreign	295	655	352	771
	1,775	2,035	1,560	2,023

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

## E) HIERARCHY OF FAIR VALUE

The following tables summarize the allocation of the fair value of the financial instruments among the three levels of the hierarchy as at December 31:

(in millions of dollars)

	Level 1	Level 2	Level 3	2010 Total
<b>Investments</b>				
<b>Fixed-income securities</b>				
Short-term investments	-	3,714	257	3,971
Bonds	-	56,021	2,514	58,535
ABTNs	-	-	7,850	7,850
Mortgages	-	4,543	3,010	7,553
<b>Total fixed-income securities</b>	-	64,278	13,631	77,909
<b>Variable-income securities</b>				
Equities and convertible securities	35,917	3,363	24,641	63,921
Real estate holdings <sup>1</sup>	-	-	21,490	21,490
<b>Total variable-income securities</b>	35,917	3,363	46,131	85,411
<b>Amounts receivable with respect to investments</b>				
Securities acquired under reverse repurchase agreements	-	9,768	-	9,768
Amount pertaining to derivative financial instruments	13	4,146	1,129	5,288
	35,930	81,555	60,891	178,376
<b>Liabilities related to investments</b>				
Securities sold under repurchase agreements	-	967	-	967
Commercial paper payable	-	1,017	-	1,017
Term notes	-	8,095	-	8,095
Short selling of securities	6,979	1,694	92	8,765
Mortgage loans payable	-	680	2,155	2,835
Other loans payable	-	2,980	13	2,993
Amount pertaining to derivative financial instruments	37	3,240	106	3,383
	7,016	18,673	2,366	28,055

1. Investments in real estate holdings include partial or full ownership of income properties through interests in a company or a partnership.

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

(in millions of dollars)				2009
	Level 1	Level 2	Level 3	Total
<b>Investments</b>				
<b>Fixed-income securities</b>				
Short-term investments	—	5,973	1,028	7,001
Bonds	—	55,809	2,793	58,602
ABTNs	—	—	7,249	7,249
Mortgages	—	3,751	5,064	8,815
<b>Total fixed-income securities</b>	—	65,533	16,134	81,667
<b>Variable-income securities</b>				
Equities and convertible securities	25,974	3,340	22,870	52,184
Real estate holdings <sup>1</sup>	—	—	19,942	19,942
<b>Total variable-income securities</b>	25,974	3,340	42,812	72,126
<b>Amounts receivable with respect to investments</b>				
Securities acquired under reverse repurchase agreements	—	8,099	—	8,099
Amount pertaining to derivative financial instruments	36	5,181	466	5,683
	26,010	82,153	59,412	167,575
<b>Liabilities related to investments</b>				
Securities sold under repurchase agreements	—	10,338	—	10,338
Commercial paper payable	—	1,288	—	1,288
Term notes	—	5,075	—	5,075
Short selling of securities	5,382	1,919	272	7,573
Mortgage loans payable	—	1,306	2,900	4,206
Other loans payable	—	1,682	313	1,995
Amount pertaining to derivative financial instruments	31	3,871	453	4,355
	5,413	25,479	3,938	34,830

1. Investments in real estate holdings include partial or full ownership of income properties through interests in a company or a partnership.

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

## LEVEL 3: RECONCILIATION BETWEEN OPENING AND CLOSING BALANCES

For the financial instruments classified in level 3 of the hierarchy, the details of the reconciliation between the opening and closing balances are as follows:

(in millions of dollars)

								2010	
	Opening balance	Total gains (losses) recorded in results <sup>1</sup>	Purchases	Sales	Issuance	Settlement	Net transfers to and from level 3	Closing balance	Total gains (losses) attributable to investments held at year-end, recorded in results <sup>2</sup>
Short-term investments	1,028	(516)	799	(17)	11	(1,048)	-	257	(124)
Bonds	2,793	(454)	829	(1,084)	400	(262)	292	2,514	(75)
ABTNs	7,249	775	-	-	-	(174)	-	7,850	1,042
Mortgages	5,064	499	-	(724)	286	(1,781)	(334)	3,010	196
Equities and convertible securities	22,870	2,608	2,774	(3,524)	-	-	(87)	24,641	864
Real estate holdings	19,942	1,197	1,592	(1,241)	-	-	-	21,490	969
Net amount pertaining to derivative financial instruments <sup>3</sup>	13	(313)	1,142	(4)	-	185	-	1,023	(104)
Short selling of securities	(272)	(28)	124	(102)	-	15	171	(92)	(1)
Mortgage loans payable	(2,900)	266	-	-	(10)	489	-	(2,155)	253
Other loans payable	(313)	(11)	-	-	(15)	326	-	(13)	361

1. Recorded under the items Investment income, Gains on the sale of investments and Unrealized increase in value.

2. Recorded under the items Investment income and Unrealized increase in value.

3. Derivative assets and derivative liabilities are recorded on a net basis in the reconciliation between opening and closing balances.

## INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

(in millions of dollars)

2009

	Opening balance	Total gains (losses) recorded in results <sup>1</sup>	Purchases	Sales	Issuance	Settlement	Net transfers to and from level 3	Closing balance	Total gains (losses) attributable to investments held at year- end, recorded in results <sup>2</sup>
Short-term investments	1,478	(267)	–	–	91	(261)	(13)	1,028	(46)
Bonds	4,654	(483)	206	(899)	(18)	(566)	(101)	2,793	(752)
ABTNs	7,231	263	–	–	–	(245)	–	7,249	454
Mortgages	6,592	(2,372)	–	(40)	1,069	(1,208)	1,023	5,064	(2,373)
Equities and convertible securities	24,269	(2,042)	2,616	(1,870)	–	–	(103)	22,870	(1,836)
Real estate holdings	22,916	(3,889)	1,633	(718)	–	–	–	19,942	(3,021)
Net amount pertaining to derivative financial instruments <sup>3</sup>	(718)	63	20	(20)	–	673	(5)	13	(140)
Short selling of securities	(460)	8	182	(2)	–	–	–	(272)	11
Mortgage loans payable	(2,632)	274	–	–	(546)	4	–	(2,900)	85
Other loans payable	(434)	15	–	–	(107)	213	–	(313)	19

1. Recorded under the items Investment income, Gains on the sale of investments and Unrealized increase in value.

2. Recorded under the items Investment income and Unrealized increase in value.

3. Derivative assets and derivative liabilities are recorded on a net basis in the reconciliation between opening and closing balances.

## LEVEL 3: VALUATION AT FAIR VALUE BASED ON REASONABLE ALTERNATIVE ASSUMPTIONS

In certain cases, the assumptions used in the valuation techniques are based on non-observable data or observable market data adjusted significantly to reflect the specific characteristics of the instrument being valued. Although the Caisse believes that its valuations at fair value are appropriate, the use of reasonably possible alternative assumptions could result in different fair values. It is possible that different entities will arrive at different valuations of the fair value of the same financial instrument on the same measurement date. Even so, the valuation techniques and input data used by both entities can meet the objective of fair value measurement. The fact that different valuations of fair value exist reflects the judgment and assumptions applied, as well as the uncertainty surrounding fair value measurement of instruments.

Substitution of reasonable alternative assumptions for the main assumptions would result in an increase of \$839 million (\$1,152 million in 2009) or a decrease of \$1,077 million (\$1,021 million in 2009) in the total fair value of the level 3 instruments, excluding ABTNs and real estate investments. The impact of such substitution on the fair value of the ABTNs is described in note 4B.

For investments in real estate holdings, the effect of using reasonable alternative assumptions has not been calculated, because the value of income property included in real estate holdings is deemed to be the only reasonable value as at the valuation date. The data used to establish the fair value of real estate holdings are not considered observable for the purposes of the hierarchy of fair value because they are not traded on active markets. However, these data are supported by market data, historical data, market transactions and/or specific contractual agreements. Valuation of the fair value of an income property, certified by external firms of real estate appraisers and carried out in accordance with professional valuation standards, represents a reasonable indication of the price that could be received at the time of the sale of income property.

## 05 DEPOSITORS' NET HOLDINGS

Demand and term deposits bear interest at variable and fixed rates, respectively, and constitute indebtedness on the part of the Caisse toward the depositors.

During the year, the Caisse paid \$3 million (\$8 million in 2009) of interest on demand deposits and term deposits.

Participation deposits are expressed in units, and each unit gives its holder a proportionate share in the net equity and the net income of a particular fund. At the end of each monthly period for the General Fund and the individual funds, the net investment income and the gains and losses on the sale of investments are allocated to participation deposit holders. At the opening of the following period, the amounts allocated are paid out to the depositors' demand deposit accounts. Generally, the balance of demand deposits is reinvested in participation deposits at the opening of each monthly period based on the investment policy of deposit holders. The number of issued units of participation deposits depends on fair value determined at the end of the previous monthly period.

During the year, the Caisse paid \$2,660 million (\$1,950 million in 2009) in net income to participation deposit holders.

(in millions of dollars)	2010	2009
Caisse's indebtedness toward depositors		
Demand deposits	197	475
Term deposits	160	9
Net income to be paid out to participation deposit holders	393	592
	750	1,076
Participation deposit holders' holdings		
Participation deposits		
Balance, beginning of year	137,123	134,015
Units issued	7,771	5,573
Units cancelled	(2,610)	(2,465)
Balance, end of year	142,284	137,123
Gains not allocated on the sale of investments	10,954	7,248
Unrealized decrease in value of investments and other related assets and liabilities	(2,246)	(13,859)
	150,992	130,512
Depositors' net holdings	151,742	131,588

The Caisse defines its capital as the net holdings of the holders of participation deposits, demand deposits and term deposits. The Caisse is not subject to external capital requirements.

The mission of the Caisse is to receive moneys on deposit as provided by the Act and to manage them with a view to achieving an optimal return on depositors' capital within the framework of their investment policies. Through its wholly owned subsidiary CDP Financial Inc., the Caisse issues capital securities to optimize financing costs and to fund certain investments.

## 06

**INVESTMENT INCOME, GAINS ON THE SALE OF INVESTMENTS AND UNREALIZED INCREASE  
IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS****A) INVESTMENT INCOME**

(in millions of dollars)	2010	2009
Fixed-income securities		
Short-term investments	165	92
Bonds	2,129	2,623
Mortgages (note 6B)	451	506
	<b>2,745</b>	<b>3,221</b>
Variable-income securities		
Equities and convertible securities	1,268	1,072
Real estate holdings (note 6C)	924	681
	<b>2,192</b>	<b>1,753</b>
Other income	13	28
Non-controlling interests	(95)	(95)
Less:		
External management fees	5	14
	<b>4,850</b>	<b>4,893</b>

Investment income – Fixed-income securities was increased by \$28 million (reduced by \$240 million in 2009) as net income (net expenses) related to securities acquired (sold) under reverse repurchase (repurchase) agreements. In addition, Short-term investments were reduced by \$6 million (\$47 million in 2009) as interest expense on commercial paper, and Bonds were reduced by \$289 million (\$34 million in 2009) as interest expense on term notes.

**B) NET INCOME FROM MORTGAGES**

(in millions of dollars)	2010	2009
Income from mortgages	416	527
Less:		
Expenses related to real estate debt subsidiaries		
Operation expenses	189	164
Financial costs of CMBS	8	18
	<b>197</b>	<b>182</b>
Other income	232	161
	<b>451</b>	<b>506</b>

# INVESTMENT INCOME, GAINS ON THE SALE OF INVESTMENTS AND UNREALIZED INCREASE IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

## C) NET INCOME FROM REAL ESTATE HOLDINGS

(in millions of dollars)	2010	2009
Income from real estate holdings	2,855	2,964
Less:		
Expenses related to real estate subsidiaries		
Operating expenses related to real estate holdings	1,352	1,532
Operation expenses	77	74
Loan financial expenses	514	681
	1,943	2,287
Other income	12	4
	924	681

## D) GAINS ON THE SALE OF INVESTMENTS

(in millions of dollars)	2010	2009
Fixed-income securities		
Short-term investments	(314)	(617)
Bonds	(659)	(710)
Mortgages	(925)	94
ABTNs	(488)	367
	(2,386)	(866)
Variable-income securities		
Equities and convertible securities	3,818	5,832
Real estate holdings	313	(359)
	4,131	5,473
Non-controlling interests	(31)	31
	1,714	4,638
Less:		
Transaction costs of investments	125	117
External management fees	7	7
	1,582	4,514

The amount of \$1,582 million of gains (\$4,514 million in 2009) on the sale of investments recorded in the Combined statement of income and changes in net assets includes \$852 million of foreign exchange gains (\$2,200 million in 2009).

**INVESTMENT INCOME, GAINS ON THE SALE OF INVESTMENTS AND UNREALIZED INCREASE IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)**
**E) UNREALIZED INCREASE IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS**

(in millions of dollars)	2010	2009
Fixed-income securities		
Short-term investments	118	(1,718)
Bonds	3,183	(6,260)
Mortgages	1,723	(2,346)
Securities acquired under reverse repurchase agreements	7	(67)
ABTNs	994	121
	6,025	(10,270)
Variable-income securities		
Equities and convertible securities	5,044	2,586
Real estate holdings	1,074	(3,452)
	6,118	(866)
Total investments	12,143	(11,136)
Less:		
Liabilities related to investments		
Securities sold under repurchase agreements	230	(294)
Commercial paper payable	—	(37)
Term notes	80	(274)
Short selling of securities	(34)	1,184
Mortgage loans payable	132	28
Other loans payable	6	51
Derivative financial instruments	(63)	(14,126)
Non-controlling interests	202	(263)
	553	(13,731)
	11,590	2,595

The unrealized increase in value in the amount of \$11,590 million (\$2,595 million in 2009) recorded in the Combined statement of income and changes in net assets includes an unrealized decrease in value of \$1,668 million related to foreign exchange (\$3,984 million in 2009).

## 07

### OPERATING EXPENSES

(in millions of dollars)	2010	2009
Salaries and employee benefits	122	117
Information technology and professional services	59	56
Data services and subscriptions	13	19
Premises and equipment	16	16
Depreciation of fixed assets	21	22
Other	14	11
	245	241
Safekeeping of securities	12	9
	257	250

## 08

### EXPENSES RELATED TO REPOSITIONING OF THE INFORMATION TECHNOLOGY AND WRITE-OFFS OF INTANGIBLE ASSETS

#### A) EXPENSES RELATED TO REPOSITIONING OF THE INFORMATION TECHNOLOGY

The combined results for 2010 include \$5.1 million of expenses relating to repositioning of information technology activities, such as costs related to design of the new business model and those arising from cancellation of consulting contracts. The balance payable at year-end of \$3 million is presented under the item Other liabilities.

#### B) WRITE-OFFS OF INTANGIBLE ASSETS

In 2010, in the context of the revision of the information technology business model, the write-offs of \$28.9 million were recorded for information technology development programs. The write-offs arise from abandonment of a corporate application *Carrefour de données* of \$15 million and the impairment of an information technology development program related to the management of the liquid investments of \$14 million that are no longer expected to provide future value.

## 09

### IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS

The Caisse has implemented a number of policies, guidelines and procedures to oversee its operations.

Risk management is based on an integrated risk management policy adopted by the Board of Directors. This policy, which is revised on a regular basis, is intended to promote a risk management culture and ensure stringent risk management practices to help the Caisse carry out its mission on behalf of its depositors. More specifically, the policy defines risk management governance within the Caisse, establishes the acceptable level of risk so as to avoid excessive loss, links the level of risk to the target value added to net assets and promotes an efficient allocation of risk.

Governance of risk management is based on three levels of control:

- Level 1 – Portfolio managers are primarily responsible for managing the risks related to operations under their purview;
- Level 2 – The Risk Committees (RC and RC – Transactions), assisted by the Risks, Policies and Compliance Department as well as by the Executive Committee; and
- Level 3 – The Board of Directors, its Audit Committee and its Risk Management Committee, as well as Internal Audit.

The policy includes reporting mechanisms for each of these levels. It also includes a framework for outsourcing management of investments, management of operational risks and management of derivative financial instruments.

To ensure the objectivity and rigour required to manage risks, teams that are independent of the portfolio managers are responsible for defining and monitoring the integrated risk management policy as well as the investment policies applying to the specialized portfolios.

The financial risks defined in the integrated risk management policy include the following:

- A) Market risk;
- B) Credit risk;
- C) Counterparty risk related to derivative financial instruments; and
- D) Financing-liquidity risk.

Investment policies oversee the activities performed by the portfolio managers. For each specialized portfolio, the investment policy defines the philosophy, management type, investment universe, benchmark index, value-added target and risk oversight, which includes concentration limits. The managers must abide by the limits specific to their investment operations.

## IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

### A) MARKET RISK

Market risk represents the risk of financial loss arising from changes in the value of financial instruments. The value of a financial instrument is affected by changes in certain market variables, such as interest rates, exchange rates, share and commodity prices, as well as their volatility. The risk derives from the volatility in the price of a financial instrument, which itself results from the volatility of such market variables.

The Caisse manages all market risks according to an integrated and comprehensive approach; the major factors contributing to risk, such as sectors, countries and issuers are taken into account in its analysis of market risk.

The Caisse may use derivative financial instruments traded on exchanges or negotiated directly with banks and securities dealers, to manage the market risks to which it is exposed.

The Caisse measures its market risk using the method known as Value at Risk (VaR), which is based on a statistical measurement of the volatility of the fair value of each position and its correlations. VaR is a statistical technique used to determine the worst loss expected during a given period according to a predetermined confidence level. The Caisse uses a 99% confidence level for its calculations. The Caisse estimates the VaR for each instrument in all the specialized portfolios and aggregates the information for the overall portfolio.

The Caisse uses the historical-simulation method to estimate VaR. The historical-simulation method is based essentially on the assumption that the future will be similar to the past. This method requires that the series of historical data on all the risk factors needed to estimate the returns on instruments be available. In the absence of historical data, alternative methods are used. A horizon of 1,300 days of observation of risk factors, such as variations in exchange rates, interest rates and financial asset prices, is used to estimate the volatility of returns and the correlation between asset returns.

The Caisse calculates two types of risk: absolute risk and active risk. The absolute risk, or absolute VaR, of the Caisse's benchmark portfolio (target portfolio of the depositors as a whole) is the result of the risk (volatility) of the benchmark indexes of the asset classes in the portfolio. For example, should the depositors as a whole elect to increase the weight of equities in their benchmark portfolios, such risk would increase automatically because of the higher level of volatility of this asset class. Consequently, the expected absolute return would also increase. The absolute risk of the overall portfolio (consisting of the actual investments) corresponds to the risk (volatility) of the positions in the Caisse's overall portfolio. The absolute risk of the overall portfolio and that of the benchmark portfolio are calculated with the same method but they relate to different portfolios, namely the overall portfolio actually invested by the Caisse and the benchmark portfolio targeted by depositors.

Active risk, or VaR related to active management, represents the possibility that the Caisse will record a return different from that of its benchmark portfolio as a result of active management of its overall portfolio. The higher the active risk, the more the absolute return expected from the overall portfolio will differ from the benchmark portfolio return.

The absolute risk of the Caisse's benchmark portfolio, the absolute risk of the overall portfolio and the active risk are measured on a regular basis.

The tables that follow show the overall portfolio's absolute risk and active risk for each category of specialized portfolios as a result of the revised portfolio offer available to depositors<sup>1</sup>, according to a 99% confidence level and a horizon of 1,300 days as at December 31:

### ABSOLUTE RISK OF THE OVERALL PORTFOLIO

(as a %)	2010	2009
Fixed Income	10.3	9.3
Inflation-Sensitive Investments	35.5	49.6
Equity	51.4	51.5
Other investments <sup>2</sup>	2.2	6.0
<b>Overall risk</b>	<b>34.3</b>	<b>38.1</b>

1. The new specialized portfolio offer available to the depositors consists of four categories of specialized portfolios: Fixed Income (Short-term Investments, Bonds, Long-term Bonds and Real Estate Debt), Inflation-Sensitive Investments (Real Return Bonds, Infrastructure and Real Estate), Equity (Canadian Equity, Global Equity, Québec International, U.S. Equity, EAFE Equity, Emerging Markets Equity and Private Equity) and Other investments (Hedge Funds, Asset Allocation and ABTNs).

2. VaR for Other investments category is presented as a percentage of net assets of the Caisse.

## IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

### ACTIVE RISK OF THE OVERALL PORTFOLIO

(as a %)	2010	2009
Fixed Income	1.3	2.8
Inflation-Sensitive Investments	11.0	20.9
Equity	6.2	7.3
Other investments <sup>1</sup>	2.1	5.8
<b>Overall risk</b>	<b>4.5</b>	<b>10.3</b>

1. VaR for Other investments category is presented as a percentage of net assets of the Caisse.

### FOREIGN EXCHANGE RISK

Foreign exchange risk represents the risk that the fair value or future cash flows of a financial instrument will fluctuate because of variations in foreign currency prices. This risk is integrated into the overall measurement of VaR.

To manage foreign exchange risk, the Caisse also uses instruments negotiated with banks. The maturities of these instruments generally range from one to 12 months for forward contracts and options, and from one to two years for foreign currency swaps. On maturity, new derivative financial instruments are negotiated to maintain effective long-term management of the foreign exchange risks associated with investments and liabilities related to investments in foreign currencies.

The tables below summarize the allocation of net investments denominated in foreign currencies as at December 31:

(in millions of dollars)							2010
	Canadian dollar	Currency <sup>a</sup>					Total
		U.S. dollar	Euro	Pound sterling	Other	Subtotal	
<b>Investments</b>							
Fixed-income securities	71,267	4,643	604	303	1,092	6,642	77,909
Equities and convertible securities	16,676	22,359	7,210	5,048	12,628	47,245	63,921
Real estate holdings	12,880	3,351	3,839	635	785	8,610	21,490
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements	8,761	1,007	—	—	—	1,007	9,768
Amount pertaining to derivative financial instruments	2,118	2,792	191	90	97	3,170	5,288
	111,702	34,152	11,844	6,076	14,602	66,674	178,376
<b>Liabilities related to investments</b>							
Conventional products <sup>b</sup>	12,042	9,408	2,735	453	34	12,630	24,672
Amount pertaining to derivative financial instruments	527	2,425	259	35	137	2,856	3,383
	12,569	11,833	2,994	488	171	15,486	28,055
Subtotal	99,133	22,319	8,850	5,588	14,431	51,188	150,321
<b>Non-controlling interests</b>	1,480	6	26	263	—	295	1,775
<b>Net investments</b>	<b>97,653</b>	<b>22,313</b>	<b>8,824</b>	<b>5,325</b>	<b>14,431</b>	<b>50,893</b>	<b>148,546</b>

a. Investments are recorded under the currency they are denominated in and are translated into Canadian dollars.

b. Conventional products include liabilities related to investments with the exception of the amount pertaining to derivative financial instruments.

# IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

(in millions of dollars)

2009

	Canadian dollar	Currency <sup>a</sup>					Total
		U.S. dollar	Euro	Pound sterling	Other	Subtotal	
<b>Investments</b>							
Fixed-income securities	72,851	5,952	1,451	466	947	8,816	81,667
Equities and convertible securities	14,078	21,011	6,127	3,392	7,576	38,106	52,184
Real estate holdings	10,930	3,146	4,197	868	801	9,012	19,942
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements	6,171	1,326	602	—	—	1,928	8,099
Amount pertaining to derivative financial instruments	1,106	3,982	379	96	120	4,577	5,683
	105,136	35,417	12,756	4,822	9,444	62,439	167,575
<b>Liabilities related to investments</b>							
Conventional products <sup>b</sup>	16,677	11,079	2,227	477	15	13,798	30,475
Amount pertaining to derivative financial instruments	442	3,431	329	36	117	3,913	4,355
	17,119	14,510	2,556	513	132	17,711	34,830
Subtotal	88,017	20,907	10,200	4,309	9,312	44,728	132,745
<b>Non-controlling interests</b>	1,208	130	30	192	—	352	1,560
<b>Net investments</b>	86,809	20,777	10,170	4,117	9,312	44,376	131,185

a. Investments are recorded under the currency they are denominated in and are translated into Canadian dollars.

b. Conventional products include liabilities related to investments with the exception of the amount pertaining to derivative financial instruments.

The impact of translation of the fair value of foreign currency investments into Canadian dollars included under the item Gains on the sale of investments and under Unrealized increase in value of investments and liabilities related to investments is unfavorable by \$2,403 million (\$6,157 million in 2009). The impact of exchange rate hedging related to a portion of such investments is favorable by \$1,587 million (\$4,373 million in 2009). The net impact on net investment results is unfavorable by \$816 million (\$1,784 million in 2009).

## INTEREST RATE RISK

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. All the interest-bearing assets and liabilities as well as their effective rates are shown in the table presenting the exposure to liquidity risk. This risk is integrated into the overall measurement of VaR.

## PRICE RISK

Price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than changes arising from interest rate risk or foreign exchange risk), whether such changes derive from the characteristics of the instrument itself or of its issuer, or from elements affecting all similar financial instruments traded on the market. This risk is integrated into the overall measurement of VaR.

## IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

### B) CREDIT RISK

Credit risk is the possibility of a loss of fair value in the event that a borrower, endorser, guarantor or counterparty does not honour its obligation to repay a loan or to fulfill any other financial commitment, or sees its financial situation deteriorate. Sources of credit risk include fixed-income securities, derivative financial instruments, provision of financial guarantees and lending commitments.

Analysis of credit risk includes the probability of default and the recovery rate on debt securities held by the Caisse, as well as monitoring of changes in the credit quality of issuers or groups of issuers held in all the specialized portfolios of the Caisse.

Analysis of concentration measures the fair value of a group of financial products, particularly fixed-income and variable-income securities, related to a single issuer or to a group of issuers<sup>1</sup> with similar characteristics (region, sector and credit rating).

The concentration limit by group of issuers is 3% of the Caisse's total assets, with the exception of securities issued by the Government of Canada, the Government of Québec or another Canadian province or territory, as well as by their departments and agencies, which are not subject to concentration limits. Sovereign issuers with an AAA credit rating are also excluded from this concentration limit. Concentration by issuer is monitored on a monthly basis or on initiation of a transaction requiring approval from the RC – Transactions Committee.

The concentration by credit rating of the Caisse's groups of issuers is as follows as at December 31:

	2010	2009
	Value as a % of investments <sup>2</sup>	
<b>Credit rating<sup>3</sup>:</b>		
AAA – AA	23.1	24.4
A	22.1	19.8
BBB	9.1	8.5
BB or lower	3.1	2.6
<b>No credit rating:</b>		
Real estate assets	17.3	17.0
ABTNs	0.6	0.7
Private equity	4.1	3.9
Private investment funds and hedge funds	7.9	8.7
Mortgages and mortgage securities	4.2	5.6
Other	8.5	8.8
	<b>100.0</b>	<b>100.0</b>

1. A group of issuers is a number of issuers under the control of a parent company.

2. The percentage of investments represents net positions by group of issuers.

3. Credit ratings are obtained from major credit rating agencies and are aggregated according to an algorithm developed in house. For the purposes of this concentration, only long-term credit ratings from major agencies are used.

In the table above, the groups of issuers for which no credit rating is available are categorized. For most of these groups, the absence of a credit rating from the main credit rating agencies is due to the private nature of the investments, the absence of any debt, restructuring of the investments or a combination of these elements. Most of the issuers, however, are evaluated with an internal rating system that is used to closely monitor changes in the credit cycle. The system includes exposure limits by sector and country (or region) and by external credit rating (no limit for internal credit ratings).

In the case of mortgages not assigned a credit rating, the analysis of credit risk is based in part on the loan-to-value ratio. In this ratio, the amount of the loan is divided by the fair value of any asset received as collateral on the subscription date or the date funds were granted, or at any other time during the term of the loan.

## IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

The table below shows the breakdown of mortgages as at December 31:

	2010	2009
	Value as a % of mortgages	
<b>Loan-to-value ratio</b>		
0 to 55%	26.5	25.4
55 to 65%	20.5	19.9
65 to 75%	35.7	18.1
75 to 85%	10.6	10.9
More than 85%	6.7	25.7
	<b>100.0</b>	<b>100.0</b>

In 2010, 142 groups of issuers whose securities are held by the Caisse received a credit upgrade from the main credit rating agencies, while 102 others received a downgrade. The Caisse frequently monitors changes in credit ratings by the agencies and compares them with the internal credit ratings.

Credit risk is measured by the fair value of investments before collateral or other credit upgrades are taken into account. For off-balance-sheet items, the value taken into account to determine maximum exposure to credit risk corresponds to the amount guaranteed or incurred.

The maximum exposure to credit risk is as follows as at December 31:

(in millions of dollars)	2010	2009
<b>Investments</b>		
Fixed-income securities	77,909	81,667
Amounts receivable with respect to investments	15,056	13,782
	<b>92,965</b>	<b>95,449</b>
<b>Off-balance-sheet</b>		
Collateral pledged (note 13)	8,843	19,550
Collaterals and loan guarantees (note 12)	1,322	707
Commitments related to ABTNs (note 12)	6,167	6,467
	<b>16,332</b>	<b>26,724</b>
<b>Total maximum exposure</b>	<b>109,297</b>	<b>122,173</b>

In reality, this exposure is less because the Caisse takes various measures to mitigate credit risk, such as the taking of guarantees (refer to note 13).

## C) COUNTERPARTY RISK RELATED TO DERIVATIVE FINANCIAL INSTRUMENTS

Over-the-counter derivative financial instruments give rise to counterparty risk, because they are negotiated by private contract without being traded through a clearing house. Counterparty risk corresponds to the credit risk from current or potential exposure arising from transactions involving this type of instrument in the event that the counterparty becomes unable to respect the conditions in the contracts.

To limit its exposure to counterparty risk arising from transactions involving over-the-counter derivative financial instruments, the Caisse carries out transactions with financial institutions whose credit rating is established by recognized credit rating agencies. Moreover, the Caisse concludes legal agreements based on the standards of the International Swaps and Derivatives Association Inc. (ISDA), which allows it to benefit from the offset between the amounts at risk and the exchange of collateral. This risk is measured by counterparty, pursuant to the legal agreement in effect, from which it is possible to calculate the net exposure created by all over-the-counter derivative financial instruments and by the collateral exchanged. Exposure to counterparty risk is measured on a daily basis, pursuant to the legal agreement in effect.

As at December 31, 2010, the legal agreements and the collateral received helped reduce exposure to the counterparty risk of over-the-counter derivative financial instruments to \$301 million (\$377 million in 2009), in respect of 68 active counterparties (78 in 2009).

## IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

### D) FINANCING-LIQUIDITY RISK

Financing-liquidity risk corresponds to the possibility that the Caisse may not always be able to fulfill the commitments related to its financial liabilities without having to obtain funds at abnormally high prices or having to sell assets.

Compliance with established rules is monitored on a monthly basis, and the liquidity status is determined daily. The Caisse uses various scenario simulations to estimate the potential impact of various market events on its liquidity. Cash managers evaluate the liquidity of the markets on which the Caisse obtains financing for its operations. They also ensure that the Caisse is active on various financial markets and maintains relationships with the credit rating agencies that rate the Caisse as well as capital providers.

The table below presents a summary of maturities at par value of investments and liabilities related to investments as at December 31:

(in millions of dollars)					2010		2009
	Less than 1 year	1 year to 5 years	More than 5 years	Total par value	Effective interest rate %	Total par value	Effective interest rate %
<b>Fixed-income securities</b>							
<b>Short-term investments</b>							
Canadian	2,406	10	—	2,416	1.9	4,826	1.4
Foreign	1,810	10	—	1,820	2.6	3,054	3.1
	4,216	20	—	4,236	2.2	7,880	2.0
<b>Bonds</b>							
<i>Issued or guaranteed by:</i>							
Government of Canada	489	10,299	9,325	20,113	2.6	20,210	2.6
Province of Québec	20	936	6,660	7,616	4.2	6,912	4.5
Other Canadian provinces	—	63	1,409	1,472	4.1	2,957	4.2
<i>Municipalities and other</i>							
Canadian agencies	152	551	550	1,253	4.5	1,278	4.6
Canadian government corporations	64	6,315	4,170	10,549	3.4	9,351	3.7
U.S. government	—	28	1,353	1,381	3.7	521	3.1
Other foreign governments	—	—	17	17	4.9	320	4.5
<i>Mortgage securities</i>							
Canadian	2	174	70	246	7.7	272	8.0
Foreign	—	48	282	330	6.2	4,073	3.9
Canadian corporations	874	2,050	5,838	8,762	5.0	10,241	4.6
Foreign corporations	1,171	572	302	2,045	8.7	2,959	7.7
<i>Inflation-indexed securities</i>							
Canadian	—	8	582	590	1.6	414	2.0
	2,772	21,044	30,558	54,374	3.7	59,508	3.9
<b>ABTNs</b>	—	281	11,686	11,967	—	12,351	—
<b>Mortgages</b>							
Canadian	1,548	2,544	1,690	5,782	4.6	6,109	5.0
Foreign	1,817	777	351	2,945	7.5	5,440	4.5
	3,365	3,321	2,041	8,727	5.6	11,549	4.8
	10,353	24,666	44,285	79,304	3.9	91,288	3.8
<b>Amounts receivable with respect to investments</b>							
<i>Securities acquired under reverse repurchase agreements</i>							
Canadian	8,763	—	—	8,763	1.0	6,171	0.3
Foreign	1,007	—	—	1,007	0.1	1,928	0.2
	9,770	—	—	9,770	0.9	8,099	0.3

## IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

(in millions of dollars)

	2010				2009	
	Less than 1 year	1 year to 5 years	More than 5 years	Total par value	Effective interest rate %	Total par value
<b>Liabilities related to investments</b>						
Securities sold under repurchase agreements	967	-	-	967	0.4	10,272
Commercial paper payable	1,019	-	-	1,019	1.1	1,289
Term notes <sup>1</sup>	-	1,987	5,981	7,968	3.8	5,242
Short selling of securities	220	1,003	408	1,631	1.5	2,018
Mortgage loans payable	133	2,135	575	2,843	4.4	4,346
Other loans payable	1,485	-	1,512	2,997	0.9	2,033
	<b>3,824</b>	<b>5,125</b>	<b>8,476</b>	<b>17,425</b>	<b>2.8</b>	<b>25,200</b>

1. In 2010, CDP Financial Inc., a wholly owned subsidiary of the Caisse, issued \$3 billion of term notes (\$5 billion in 2009).

The Caisse is a party to various commitments and issues financial guarantees that can have an impact on its liquidity (refer to notes 4B, 12 and 13).

## 10 DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are financial contracts whose value fluctuates as a function of the underlying asset, and which do not require holding or delivering the underlying asset itself. This underlying may be of a financial nature (interest rate, foreign currency or stock market security or index) or a commodity (precious metal, produce or crude oil).

The notional amount of a derivative financial instrument represents the value of the notional principal to which a rate or a price applies to determine the exchange of future cash flows, and does not reflect the credit risk pertaining to the instrument.

The Caisse uses derivative financial instruments that include the following:

- Forward contracts and futures contracts are undertakings that enable the purchase or sale of an underlying, the quantity and price of which are determined in the contract, which includes a predetermined maturity date. A forward contract involves customized conditions negotiated directly between the parties on the over-the-counter market. A futures contract has terms and conditions determined by an organized market.
- A swap is a transaction whereby two parties agree to exchange financial flows on predetermined conditions that include a notional amount and a term.
- An option is a contract that is negotiated by mutual agreement or traded on an organized market and that gives the purchaser the right, but not the obligation, to buy or sell a given amount of an underlying security, index or commodity, at a strike price stipulated in advance, either at a determined date or at any time before a specified maturity date.

Foreign exchange risk arises from investments and liabilities related to investments denominated in foreign currencies, as well as from related derivative financial instruments.

Derivative financial instruments that are traded on exchanges or negotiated with banks and securities dealers are used to manage the interest rate and market risks of the total investment portfolio.

## DERIVATIVE FINANCIAL INSTRUMENTS (cont.)

## A) SUMMARY OF DERIVATIVE FINANCIAL INSTRUMENTS

(in millions of dollars)

(in millions of dollars)				2010	2009
	Notional amount	Fair value		Net amount	Net amount
		Assets	Liabilities		
<b>Foreign exchange risk management</b>					
Foreign currency swaps					
Purchases	2,266	170	—	170	121
Sales	99	2	1	1	(54)
Forward contracts					
Purchases	2,272	3	71	(68)	(30)
Sales	16,932	586	44	542	948
Over-the-counter foreign currency options					
Purchases	158	—	—	—	1
Sales	34	—	—	—	—
	21,761	761	116	545	986
<b>Interest rate and market risk management</b>					
Interest rate and foreign currency swaps	84,770	2,946	2,909	37	169
Credit default swaps	42,321	1,119	24	1,095	(117)
Equity and convertible securities swaps	17,262	235	115	120	347
Commodity swaps	74	4	7	(3)	(86)
Futures contracts	14,432	7	35	(28)	—
Forward contracts	8,154	66	81	(15)	(16)
Over-the-counter options					
Purchases	6,534	65	—	65	685
Sales	2,619	—	86	(86)	(670)
Exchange-traded options					
Purchases	772	24	—	24	36
Sales	454	—	10	(10)	(31)
Warrants	115	61	—	61	25
	177,507	4,527	3,267	1,260	342
<b>Total derivative financial instrument contracts</b>	<b>199,268</b>	<b>5,288</b>	<b>3,383</b>	<b>1,905</b>	<b>1,328</b>

## DERIVATIVE FINANCIAL INSTRUMENTS (cont.)

## B) SUMMARY OF DERIVATIVE FINANCIAL INSTRUMENT MATURITIES

(in millions of dollars)				2010	2009
	Notional amount – Maturity				
	Less than 1 year	1 year to 5 years	More than 5 years	Total	Notional amount
<b>Foreign exchange risk management</b>					
Foreign currency swaps					
Purchases	400	1,733	133	2,266	1,605
Sales	59	40	–	99	859
Forward contracts					
Purchases	2,272	–	–	2,272	5,519
Sales	16,073	789	70	16,932	29,824
Over-the-counter foreign currency options					
Purchases	158	–	–	158	178
Sales	34	–	–	34	39
	18,996	2,562	203	21,761	38,024
<b>Interest rate and market risk management</b>					
Interest rate and foreign currency swaps	11,711	48,222	24,837	84,770	86,099
Credit default swaps	465	34,562	7,294	42,321	4,411
Equity and convertible securities swaps	17,230	32	–	17,262	16,091
Commodity swaps	56	18	–	74	5,533
Futures contracts	14,432	–	–	14,432	19,880
Forward contracts	8,140	14	–	8,154	6,753
Over-the-counter options					
Purchases	5,709	825	–	6,534	14,431
Sales	2,276	343	–	2,619	9,277
Exchange-traded options					
Purchases	772	–	–	772	936
Sales	454	–	–	454	618
Warrants	77	38	–	115	51
	61,322	84,054	32,131	177,507	164,080
<b>Total derivative financial instrument contracts</b>	<b>80,318</b>	<b>86,616</b>	<b>32,334</b>	<b>199,268</b>	<b>202,104</b>

(in millions of dollars)					2010	2009
	Fair value – Maturity					
	Less than 1 year	1 year to 5 years	More than 5 years	Total		Notional amount
<b>Derivative financial instruments</b>						
Assets	1,028	3,034	1,226	5,288		5,683
Liabilities	412	2,026	945	3,383		4,355
<b>Net amount</b>	<b>616</b>	<b>1,008</b>	<b>281</b>	<b>1,905</b>		<b>1,328</b>

# 11

## TRANSFERS OF RECEIVABLES

The Caisse has put in place a program to syndicate some of its mortgages. Pursuant to these transactions, the Caisse assumes the role of administrator of the mortgages sold and thus maintains a relationship with clients. During the year ended December 31, 2010, the Caisse carried out various syndication operations totalling \$231 million (\$126 million in 2009), which met the criteria set out in AcG-12 and were therefore recorded as sales.

No securitization activities were carried out in 2010 and 2009.

# 12

## COMMITMENTS AND CONTINGENCIES

Given the nature of its operations, the Caisse has a number of commitments.

Commitments to buy investments mean the Caisse is committed to buying investments that will be settled in the coming financial years, in accordance with the terms and conditions in each agreement.

For the Caisse, guarantees and loan guarantees consist in providing guarantees to financial institutions and corporations regarding future income deriving from the sale of investments and transactions on derivative financial instruments as well as repayment of loans made by investee companies. Guarantees related to the repayment of loans have no specific maturity date, except in some cases where the terms range from one to seven years.

(in millions of dollars)	2010	2009
Commitments to buy investments	6,902	12,129
Guarantees and loan guarantees	1,322	707
ABTNs <sup>1</sup>	6,167	6,467
	14,391	19,303

1. For the description of the commitments related to ABTNs, refer to note 4B.

## 13

### COLLATERALS

In the normal course of business, the Caisse pledges financial assets as collateral for securities borrowed, securities sold under repurchase agreements and transactions involving derivative financial instruments. The counterparty is authorized to sell or pledge as collateral certain securities in the absence of default by the Caisse. On certain conditions, the Caisse may have to pledge additional collateral if collateral already pledged has lost value.

The following table presents the fair value of the collateral pledged by the Caisse as at December 31:

(in millions of dollars)	2010	2009
Collateral pledged for		
Securities borrowed	<b>6,905</b>	6,469
Securities sold under repurchase agreements	<b>967</b>	11,743
Over-the-counter derivative financial instruments	<b>—</b>	59
Listed derivative financial instruments	<b>971</b>	1,279
	<b>8,843</b>	19,550

The Caisse receives financial assets as collateral for securities lent, securities acquired under reverse repurchase agreements and transactions involving derivative financial instruments. The Caisse is authorized to sell or pledge certain securities in the absence of default by the counterparty. The Caisse is obliged to return such securities to the counterparties. If the value of the collateral received decreases, the Caisse may, in certain cases, request additional collateral.

The following table presents the fair value of the collateral received by the Caisse as at December 31:

(in millions of dollars)	2010	2009
Collateral received for		
Securities lent	<b>2,108</b>	2,104
Securities acquired under reverse repurchase agreements	<b>9,784</b>	8,084
Over-the-counter derivative financial instruments	<b>1,926</b>	1,818
	<b>13,818</b>	12,006

## 14

### COMPARATIVE FIGURES

Certain figures from the 2009 financial statements have been reclassified to conform to the presentation adopted in 2010.

### SUPPLEMENTARY INFORMATION

Summary financial statements for the specialized portfolios

(in millions of dollars)

(In millions of dollars)	SHORT TERM INVESTMENTS (740)		BONDS (760)	LONG TERM BONDS (764)		REAL ESTATE DEBT (750)		
	2010	2009	2010	2009	2010	2009	2010	2009
<b>Consolidated net assets as at December 31</b>								
<b>Assets</b>								
Investments at fair value								
Real estate holdings	-	-	-	-	-	-	-	-
Equities and convertible securities	-	-	-	-	-	-	-	-
Bonds	-	-	51,495.2	54,653.6	3,571.5	3,227.2	-	-
Mortgages	-	-	-	-	-	-	6,609.2	8,156.8
Mortgage securities	-	-	-	-	-	-	281.0	579.4
Short-term investments	-	2,726.7	2,979.2	10,405.6	741.0	-	1,048.1	15.0
Securities acquired under reverse repurchase agreements	3,209.2	-	10,791.8	11,907.8	-	145.7	-	-
Real estate held for resale	-	-	-	-	-	-	24.7	272.7
ABTNs	-	-	-	7,249.3	-	-	-	-
Derivative financial instruments related to ABTNs	-	-	-	5,122.0	-	-	-	-
Demand deposits in the General Fund	167.1	-	-	-	-	855.1	-	524.1
	3,376.3	2,726.7	65,266.2	89,338.3	4,312.5	4,228.0	7,963.0	9,548.0
Other assets	-	1.0	1,273.6	1,483.5	43.2	28.1	1,065.5	715.1
	3,376.3	2,727.7	66,539.8	90,821.8	4,355.7	4,256.1	9,028.5	10,263.1
<b>Liabilities</b>								
Advances from the General Fund	-	12.8	979.3	10,101.7	5.9	-	18.5	-
Securities sold under repurchase agreements	-	-	5,030.5	10,113.6	741.0	1,069.7	-	-
Notes payable	-	-	12,318.9	19,814.2	-	-	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-	-	-
Loans payable	-	-	-	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-	-	-	238.5
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-	13.4	249.1
Participating debenture	-	-	-	-	-	-	-	74.2
Short selling of securities	-	-	4,611.2	8,609.7	-	84.0	-	-
Derivative financial instruments	-	-	3,062.5	2,881.5	-	-	166.0	267.2
Other liabilities	3.1	1.3	829.4	1,927.5	22.8	11.5	123.6	136.9
Non-controlling interests	-	-	-	-	-	-	71.1	18.3
	3.1	14.1	26,631.8	53,448.2	769.7	1,165.2	392.6	1,216.6
<b>Net holdings of funds</b>	<b>3,373.2</b>	<b>2,713.6</b>	<b>39,908.0</b>	<b>37,373.6</b>	<b>3,586.0</b>	<b>3,090.9</b>	<b>8,635.9</b>	<b>9,046.5</b>
<b>Consolidated income for years ended December 31</b>								
<b>Income</b>								
Investment income								
Real estate holdings	-	-	-	-	-	-	-	-
Equities and convertible securities	-	-	-	-	-	-	-	-
Bonds	-	-	1,565.2	2,270.8	141.3	134.0	-	-
Mortgages	-	-	-	-	-	-	608.2	267.0
Mortgage securities	-	-	-	-	-	-	-	-
Short-term investments	19.0	28.4	114.5	247.4	0.2	-	1.4	0.1
Demand deposits in (advances from) the General Fund	(0.2)	(0.1)	(2.5)	(10.9)	(0.1)	-	0.1	13.6
	18.8	28.3	1,677.2	2,507.3	141.4	134.0	609.7	280.7
Other income	-	-	-	-	-	-	-	-
	18.8	28.3	1,677.2	2,507.3	141.4	134.0	609.7	280.7
Operating expenses	0.5	0.5	39.1	42.4	1.8	1.3	7.2	8.3
Repositioning expenses and write-offs of intangible assets	0.1	-	7.1	-	0.2	-	0.4	-
<b>Income before the following items</b>	<b>18.2</b>	<b>27.8</b>	<b>1,631.0</b>	<b>2,464.9</b>	<b>139.6</b>	<b>132.7</b>	<b>602.1</b>	<b>272.4</b>
Interest on loans and notes payable	-	-	82.9	113.7	-	-	-	-
Non-controlling interests	-	-	-	-	-	-	6.3	4.5
<b>Net investment income (loss)</b>	<b>18.2</b>	<b>27.8</b>	<b>1,548.1</b>	<b>2,351.2</b>	<b>139.6</b>	<b>132.7</b>	<b>595.8</b>	<b>267.9</b>
<b>Changes in consolidated net assets for years ended December 31</b>								
<b>Net investment results</b>								
Net investment income (loss)	18.2	27.8	1,548.1	2,351.2	139.6	132.7	595.8	267.9
Gains (losses) on sale of investments	0.2	13.6	672.8	(61.3)	192.2	(7.6)	(2,984.7)	(109.5)
Unrealized increase (decrease) in value of investments and liabilities related to investments	(0.1)	(0.5)	939.9	203.7	58.7	(62.4)	3,765.0	(2,469.9)
Net investment results	18.3	40.6	3,160.8	2,493.6	390.5	62.7	1,376.1	(2,311.5)
Participation units issued (cancelled)	659.5	(1,761.2)	921.7	(7,090.0)	244.2	132.8	(1,190.9)	714.6
Net investment loss (net income) recovered from (allocated to) participation unit holders	(18.2)	(27.8)	(1,548.1)	(2,351.2)	(139.6)	(132.7)	(595.8)	(267.9)
<b>Increase (decrease) in consolidated net assets</b>	<b>659.6</b>	<b>(1,748.4)</b>	<b>2,534.4</b>	<b>(6,937.6)</b>	<b>495.1</b>	<b>62.8</b>	<b>(410.6)</b>	<b>(1,864.8)</b>
<b>Consolidated net assets, beginning of year</b>	<b>2,713.6</b>	<b>4,462.0</b>	<b>37,373.6</b>	<b>44,311.2</b>	<b>3,090.9</b>	<b>3,028.1</b>	<b>9,046.5</b>	<b>10,911.3</b>
<b>Consolidated net assets, end of year</b>	<b>3,373.2</b>	<b>2,713.6</b>	<b>39,908.0</b>	<b>37,373.6</b>	<b>3,586.0</b>	<b>3,090.9</b>	<b>8,635.9</b>	<b>9,046.5</b>
<b>Investments and liabilities at cost as at December 31</b>								
<b>Assets</b>								
Investments								
Real estate holdings	-	-	-	-	-	-	-	-
Equities and convertible securities	-	-	-	-	-	-	-	-
Bonds	-	-	48,400.3	52,577.2	3,534.9	3,249.4	-	-
Mortgages	-	-	-	-	-	-	7,490.9	10,779.9
Mortgage securities	-	-	-	-	-	-	544.6	2,561.3
Short-term investments	-	2,726.6	2,055.6	9,712.4	741.0	-	1,048.1	15.0
Securities acquired under reverse repurchase agreements	3,209.2	-	10,802.6	11,917.4	-	145.7	-	-
Real estate held for resale	-	-	-	-	-	-	46.3	546.4
ABTNs	-	-	-	12,350.5	-	-	-	-
Demand deposits in the General Fund	167.1	-	-	-	-	855.1	-	524.1
	3,376.3	2,726.6	61,258.5	86,557.5	4,275.9	4,250.2	9,129.9	14,426.7
<b>Liabilities</b>								
Securities sold under repurchase agreements	-	-	5,042.9	10,112.3	741.0	1,069.7	-	-
Notes payable	-	-	12,318.9	19,846.6	-	-	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-	-	-
Loans payable	-	-	-	-	-	-	-	247.7
Mortgage loans payable	-	-	-	-	-	-	-	278.7
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-	13.5	246.1
Participating debenture	-	-	-	-	-	-	-	99.9
Short selling of securities	-	-	4,619.4	8,644.7	-	84.0	-	-
Derivative financial instruments	-	-	283.4	344.0	-	-	82.7	0.5
Non-controlling interests	-	-	-	-	-	-	43.4	29.4

## SUPPLEMENTARY INFORMATION

## Summary financial statements for the specialized portfolios (cont.)

(in millions of dollars)

	REAL RETURN BONDS (762)		INFRA- STRUCTURE (762) (Growth July 1, 2010)	REAL ESTATE (710)		CANADIAN EQUITY (720)	
	2010	2009	2010	2010	2009	2010	2009
<b>Consolidated net assets as at December 31</b>							
<b>Assets</b>							
Investments at fair value							
Real estate holdings	-	-	-	21,618.0	19,831.8	-	-
Equities and convertible securities	-	-	4,475.7	4,232.4	4,149.1	11,490.8	12,549.9
Bonds	975.3	667.1	501.4	-	-	-	-
Mortgages	-	-	-	1,199.0	680.3	-	-
Mortgage securities	-	-	-	-	92.5	-	-
Short-term investments	-	-	-	1,174.4	3,288.5	13,854.8	9,100.9
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-	-
Derivative financial instruments related to ABTNs	-	-	-	-	-	-	-
Demand deposits in the General Fund	3.5	-	147.7	-	-	-	-
	978.8	667.1	5,124.8	28,223.8	28,042.2	25,345.6	21,650.8
Other assets	2.1	8.2	33.2	1,801.8	893.4	36.4	23.6
	980.9	675.3	5,158.0	30,025.6	28,935.6	25,382.0	21,674.4
<b>Liabilities</b>							
Advances from the General Fund	-	22.5	-	222.8	51.5	395.3	467.5
Securities sold under repurchase agreements	6.5	-	-	-	-	-	-
Notes payable	-	-	-	-	200.0	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-	-
Loans payable	-	-	12.8	8,305.5	8,421.2	-	-
Mortgage loans payable	-	-	-	2,835.1	3,973.9	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-	-
Short selling of securities	-	-	-	-	-	5,573.1	4,075.3
Derivative financial instruments	-	-	102.6	314.6	430.8	40.2	26.6
Other liabilities	38.7	0.6	13.6	879.0	761.0	110.9	98.8
Non-controlling interests	-	-	709.8	894.6	909.0	-	-
	45.2	23.1	838.8	13,551.6	14,747.4	6,119.5	4,698.2
<b>Net holdings of funds</b>	<b>935.7</b>	<b>652.2</b>	<b>4,319.2</b>	<b>16,474.0</b>	<b>14,188.2</b>	<b>19,262.5</b>	<b>17,006.2</b>
<b>Consolidated income for years ended December 31</b>							
<b>Income</b>							
Investment income							
Real estate holdings	-	-	-	607.7	521.1	-	-
Equities and convertible securities	-	-	74.3	15.4	10.3	373.0	396.9
Bonds	26.6	13.5	7.0	-	-	-	-
Mortgages	-	-	-	45.9	38.8	-	-
Mortgage securities	-	-	-	4.5	6.2	-	-
Short-term investments	-	-	-	52.0	71.4	89.5	65.1
Demand deposits in (advances from) the General Fund	(0.1)	(0.3)	2.2	(0.3)	(0.4)	(3.5)	(0.8)
	26.5	13.2	83.5	725.2	647.4	459.0	451.2
Other income	-	-	2.3	-	-	-	-
	26.5	13.2	85.8	725.2	647.4	459.0	451.2
Operating expenses	0.5	0.3	11.4	17.2	15.8	40.0	35.0
Repositioning expenses and write-offs of intangible assets	0.1	-	2.3	0.9	-	5.5	-
<b>Income before the following items</b>	<b>25.9</b>	<b>12.9</b>	<b>72.1</b>	<b>707.1</b>	<b>631.6</b>	<b>413.5</b>	<b>416.2</b>
Interest on loans and notes payable	-	-	-	-	-	0.3	-
Non-controlling interests	-	-	12.5	60.8	60.5	-	-
<b>Net investment income (loss)</b>	<b>25.9</b>	<b>12.9</b>	<b>59.6</b>	<b>646.3</b>	<b>571.1</b>	<b>413.2</b>	<b>416.2</b>
<b>Changes in consolidated net assets for years ended December 31</b>							
<b>Net investment results</b>							
Net investment income (loss)	25.9	12.9	59.6	646.3	571.1	413.2	416.2
Gains (losses) on sale of investments	22.3	16.3	32.1	285.9	(6.3)	1,089.2	1,945.6
Unrealized increase (decrease) in value of investments and liabilities related to investments	32.3	65.8	354.9	1,027.9	(2,364.4)	1,054.4	2,205.3
Net investment results	80.5	95.0	446.6	1,960.1	(1,799.6)	2,556.8	4,567.1
Participation units issued (cancelled)	228.9	8.5	3,932.2	972.0	2,625.1	112.7	28.5
Net investment loss (net income) recovered from (allocated to) participation unit holders	(25.9)	(12.9)	(59.6)	(646.3)	(571.1)	(413.2)	(416.2)
<b>Increase (decrease) in consolidated net assets</b>	<b>283.5</b>	<b>90.6</b>	<b>4,319.2</b>	<b>2,285.8</b>	<b>254.4</b>	<b>2,256.3</b>	<b>4,179.4</b>
<b>Consolidated net assets, beginning of year</b>	<b>652.2</b>	<b>561.6</b>	<b>-</b>	<b>14,188.2</b>	<b>13,933.8</b>	<b>17,006.2</b>	<b>12,826.8</b>
<b>Consolidated net assets, end of year</b>	<b>935.7</b>	<b>652.2</b>	<b>4,319.2</b>	<b>16,474.0</b>	<b>14,188.2</b>	<b>19,262.5</b>	<b>17,006.2</b>
<b>Investments and liabilities at cost as at December 31</b>							
<b>Assets</b>							
Investments							
Real estate holdings	-	-	-	20,092.3	19,151.7	-	-
Equities and convertible securities	-	-	4,074.0	4,036.1	4,195.0	8,400.5	10,712.1
Bonds	895.8	619.9	483.0	-	-	-	-
Mortgages	-	-	-	1,220.7	751.4	-	-
Mortgage securities	-	-	-	-	104.8	-	-
Short-term investments	-	-	-	1,174.5	3,287.2	13,843.3	9,096.6
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-	-
Demand deposits in the General Fund	3.5	-	147.7	-	-	-	-
	899.3	619.9	4,704.7	26,523.6	27,490.1	22,243.8	19,807.7
<b>Liabilities</b>							
Securities sold under repurchase agreements	6.5	-	-	-	-	-	-
Notes payable	-	-	-	-	200.0	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-	-
Loans payable	-	-	13.2	8,409.1	8,601.1	-	-
Mortgage loans payable	-	-	-	2,842.9	4,067.9	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-	-
Short selling of securities	-	-	-	-	-	4,749.3	3,442.0
Derivative financial instruments	-	-	99.9	17.1	26.9	-	0.3
Non-controlling interests	-	-	647.0	1,027.0	982.6	-	-

## SUPPLEMENTARY INFORMATION

Summary financial statements for the specialized portfolios (cont.)

(in millions of dollars)

	GLOBAL EQUITY (738) (Created April 1, 2010)	QUÉBEC INTERNATIONAL (781) 2009	U.S. EQUITY (731) (Created April 1, 2010)	EAFE EQUITY (730) (Created April 1, 2010)	EMERGING MARKETS EQUITY (732)
	2010	2010	2010	2010	2010
<b>Consolidated net assets as at December 31</b>					
<b>Assets</b>					
Investments at fair value					
Real estate holdings	-	-	-	-	-
Equities and convertible securities	9,520.1	8.1	134.3	547.0	9,722.6
Bonds	9.1	6,843.4	10,211.8	-	5,809.3
Mortgages	-	-	-	-	4,946.0
Mortgage securities	-	-	-	-	-
Short-term investments	30.2	1,972.2	2,726.2	5,279.0	0.1
Securities acquired under reverse repurchase agreements	-	-	853.2	-	-
Real estate held for resale	-	-	-	-	-
ABTNs	-	-	-	-	-
Derivative financial instruments related to ABTNs	-	-	-	-	-
Demand deposits in the General Fund	-	219.7	3,624.1	-	-
	9,559.4	9,043.4	17,549.6	5,826.0	5,809.3
Other assets	49.2	66.0	86.7	1.1	19.5
	9,608.6	9,109.4	17,636.3	5,827.1	5,815.6
<b>Liabilities</b>					
Advances from the General Fund	58.7	-	-	68.2	4.9
Securities sold under repurchase agreements	-	281.1	3,812.4	-	6.1
Notes payable	1,444.7	-	234.4	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-
Loans payable	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-
Participating debenture	-	-	-	-	-
Short selling of securities	2,082.5	-	0.7	-	6.2
Derivative financial instruments	99.3	0.3	21.1	-	-
Other liabilities	57.0	398.2	768.4	0.3	8.4
Non-controlling interests	-	-	-	-	4.2
	3,742.2	679.6	4,837.0	66.5	13.2
<b>Net holdings of funds</b>	<b>5,866.4</b>	<b>8,429.8</b>	<b>12,799.3</b>	<b>5,760.6</b>	<b>5,799.1</b>
<b>Consolidated income for years ended December 31</b>					
<b>Income</b>					
Investment income					
Real estate holdings	-	-	-	-	-
Equities and convertible securities	99.8	0.3	0.4	9.9	185.9
Bonds	-	303.4	290.3	-	110.6
Mortgages	-	-	-	-	82.4
Mortgage securities	-	-	-	-	-
Short-term investments	0.1	11.2	13.9	12.5	-
Demand deposits in (advances from) the General Fund	(0.2)	(0.2)	(2.5)	0.1	(0.1)
	99.7	314.7	302.1	22.5	185.7
Other income	-	-	-	-	110.5
	99.7	314.7	302.1	22.5	185.7
Operating expenses	11.3	32.0	19.8	3.9	7.3
Repositioning expenses and write-offs of intangible assets	2.5	5.1	-	0.7	1.2
<b>Income before the following items</b>	<b>85.9</b>	<b>277.6</b>	<b>282.3</b>	<b>17.9</b>	<b>177.2</b>
Interest on loans and notes payable	6.3	0.1	2.8	-	-
Non-controlling interests	-	-	-	-	-
<b>Net investment income (loss)</b>	<b>79.6</b>	<b>277.5</b>	<b>279.5</b>	<b>17.9</b>	<b>177.2</b>
<b>Changes in consolidated net assets for years ended December 31</b>					
<b>Net investment results</b>					
Net investment income (loss)	79.6	277.5	279.5	17.9	177.2
Gains (losses) on sale of investments	(108.7)	792.2	2,766.8	333.9	(99.1)
Unrealized increase (decrease) in value of investments and liabilities related to investments	534.1	109.7	(78.4)	20.3	497.1
Net investment results	505.0	1,179.4	2,967.9	372.1	575.2
Participation units issued (cancelled)	5,441.0	(5,271.4)	5,890.4	5,406.4	9,331.0
Net investment loss (net income) recovered from (allocated to) participation unit holders	(79.6)	(277.5)	(279.5)	(17.9)	(177.2)
<b>Increase (decrease) in consolidated net assets</b>	<b>5,866.4</b>	<b>(4,369.5)</b>	<b>8,579.4</b>	<b>5,760.6</b>	<b>9,729.0</b>
<b>Consolidated net assets, beginning of year</b>	<b>-</b>	<b>12,799.3</b>	<b>4,219.9</b>	<b>-</b>	<b>4,938.3</b>
<b>Consolidated net assets, end of year</b>	<b>5,866.4</b>	<b>8,429.8</b>	<b>12,799.3</b>	<b>5,760.6</b>	<b>5,799.1</b>
<b>Investments and liabilities at cost as at December 31</b>					
<b>Assets</b>					
Investments					
Real estate holdings	-	-	-	-	-
Equities and convertible securities	8,893.1	-	129.2	447.4	9,225.6
Bonds	10.0	6,752.6	10,194.1	-	4,638.1
Mortgages	-	-	-	-	4,045.4
Mortgage securities	-	-	-	-	-
Short-term investments	-	1,971.9	2,742.7	5,358.2	-
Securities acquired under reverse repurchase agreements	-	-	853.2	-	-
Real estate held for resale	-	-	-	-	-
ABTNs	-	-	-	-	-
Demand deposits in the General Fund	-	219.7	3,624.1	-	-
	8,903.1	8,944.2	17,543.3	5,805.6	9,225.6
<b>Liabilities</b>					
Securities sold under repurchase agreements	-	281.1	3,812.3	-	-
Notes payable	1,444.7	-	235.7	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-
Loans payable	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-
Participating debenture	-	-	-	-	-
Short selling of securities	2,055.9	-	0.4	-	6.1
Derivative financial instruments	3.7	-	2.9	-	-
Non-controlling interests	-	-	-	-	-
	3,504.3	281.1	4,051.3	3,504.3	54.4

## SUPPLEMENTARY INFORMATION

## Summary financial statements for the specialized portfolios (cont.)

(in millions of dollars)

	PRIVATE EQUITY (780)		HEDGE FUNDS (770)		ASSET ALLOCATION (771)		ABTNs (772)
	2010	2009	2010	2009	2010	2009	(Audited January 1, 2010) 2010
<b>Consolidated net assets as at December 31</b>							
<b>Assets</b>							
Investments at fair value							
Real estate holdings	-	-	-	-	-	-	-
Equities and convertible securities	16,257.0	11,980.7	3,243.0	3,619.9	32.8	20.1	-
Bonds	461.2	375.8	-	21.8	79.8	103.5	-
Mortgages	-	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-	-
Short-term investments	131.8	270.4	8.0	106.8	159.6	-	-
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-	8,941.6
Derivative financial instruments related to ABTNs	-	-	-	-	-	-	-
Demand deposits in the General Fund	713.9	381.8	155.4	82.2	667.8	428.6	3.4
	17,563.9	13,008.7	3,406.4	3,830.7	940.0	562.2	8,945.0
Other assets	37.8	13.4	6.1	3.8	2.8	0.3	37.4
	17,601.7	13,022.1	3,412.5	3,834.5	942.8	562.5	8,982.4
<b>Liabilities</b>							
Advances from the General Fund	-	-	-	-	-	-	-
Securities sold under repurchase agreements	-	-	-	-	-	-	-
Notes payable	-	1,060.6	-	-	-	-	10,004.1
Temporary funding attributable to foreign currency fluctuations	-	599.9	-	-	-	-	-
Loans payable	-	-	-	-	-	-	1,503.3
Mortgage loans payable	-	-	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-	-
Short selling of securities	91.9	100.9	-	-	-	-	-
Derivative financial instruments	3.3	2.6	99.3	-	308.1	52.6	25.2
Other liabilities	59.0	23.2	7.4	8.0	-	0.5	60.6
Non-controlling interests	-	-	-	-	-	-	-
	154.2	1,787.2	106.7	8.0	308.1	53.1	11,593.2
<b>Net holdings of funds</b>	17,447.5	11,234.9	3,305.8	3,826.5	634.7	499.4	(2,610.8)
<b>Consolidated income for years ended December 31</b>							
<b>Income</b>							
Investment income							
Real estate holdings	-	-	-	-	-	-	-
Equities and convertible securities	173.4	86.4	(0.1)	3.4	(0.1)	-	-
Bonds	49.3	61.4	-	(0.1)	(2.0)	8.9	-
Mortgages	-	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-	-
Short-term investments	19.7	46.0	-	-	-	-	-
ABTNs	-	-	-	-	-	-	111.1
Demand deposits in (advances from) the General Fund	2.1	(0.2)	0.4	(6.4)	2.0	2.0	0.1
Other income	244.5	193.6	0.3	(3.1)	(0.1)	10.9	111.2
	2.1	4.5	-	-	-	-	-
	246.6	198.1	0.3	(3.1)	(0.1)	10.9	111.2
Operating expenses	25.6	19.7	10.2	12.8	9.5	9.1	9.6
Repositioning expenses and write-offs of intangible assets	2.7	-	1.2	-	1.3	-	0.8
<b>Income before the following items</b>	218.3	178.4	(11.1)	(15.9)	(10.9)	1.8	100.8
Interest on loans and notes payable	3.6	23.5	-	-	-	2.0	91.6
Non-controlling interests	-	-	-	-	-	-	-
<b>Net investment income (loss)</b>	214.7	154.9	(11.1)	(15.9)	(10.9)	(0.2)	9.2
<b>Changes in consolidated net assets for years ended December 31</b>							
<b>Net investment results</b>							
Net investment income (loss)	214.7	154.9	(11.1)	(15.9)	(10.9)	(0.2)	9.2
Gains (losses) on sale of investments	849.3	708.1	135.4	219.8	(46.3)	(609.1)	(499.8)
Unrealized increase (decrease) in value of investments and liabilities related to investments	2,241.7	218.8	75.6	230.9	(20.0)	642.6	999.6
Net investment results	3,305.7	1,081.8	199.9	434.8	(77.2)	33.3	509.0
Participation units issued (cancelled)	3,121.6	587.7	(731.7)	(560.4)	201.6	391.0	2,011.4
Transfer of unrealized decrease at January 1, 2010	-	-	-	-	-	-	(5,122.0)
Net investment loss (net income) recovered from (allocated to) participation unit holders	(214.7)	(151.8)	11.1	15.9	10.9	(0.2)	(9.2)
<b>Increase (decrease) in consolidated net assets</b>	6,212.6	1,517.7	(520.7)	(109.7)	135.3	424.5	(2,610.8)
<b>Consolidated net assets, beginning of year</b>	11,234.9	9,717.2	3,826.5	3,930.2	499.4	74.9	-
<b>Consolidated net assets, end of year</b>	17,447.5	11,234.9	3,305.8	3,820.5	634.7	524.4	(2,610.8)
<b>Investments and liabilities at cost as at December 31</b>							
<b>Assets</b>							
Investments							
Real estate holdings	-	-	-	-	-	-	-
Equities and convertible securities	18,777.5	16,605.9	3,070.5	3,627.6	11.6	31.7	-
Bonds	660.9	663.9	-	22.0	-	79.0	-
Mortgages	-	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-	-
Short-term investments	199.2	398.1	8.0	101.3	49.5	-	-
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-	13,049.6
Demand deposits in the General Fund	713.9	381.8	155.4	82.2	667.8	428.6	3.4
	20,351.5	18,049.7	3,233.9	3,813.1	728.9	539.3	13,053.0
<b>Liabilities</b>							
Securities sold under repurchase agreements	-	-	-	-	-	-	-
Notes payable	-	1,044.9	-	-	-	-	10,005.0
Temporary funding attributable to foreign currency fluctuations	-	600.0	-	-	-	-	-
Loans payable	-	-	-	-	-	-	1,511.7
Mortgage loans payable	-	-	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-	-
Short selling of securities	90.5	76.2	-	-	-	-	-
Derivative financial instruments	-	-	-	-	37.4	-	1.6
Non-controlling interests	-	-	-	-	-	-	-

## SUPPLEMENTARY INFORMATION

Summary financial statements for the specialized portfolios (cont.)

(in millions of dollars)

Consolidated net assets as at December 31	FOREIGN EQUITY HEDGED (730) (Billion April 1, 2010)		U.S. EQUITY HEDGED (731) (Billion April 1, 2010)		FOREIGN EQUITY UNHEDGED (738) (Billion April 1, 2010)	
	2010	2009	2010	2009	2010	2009
<b>Assets</b>						
Investments at fair value						
Real estate holdings	-	-	-	-	-	-
Equities and convertible securities	-	7,514.8	-	1,723.9	-	-
Bonds	-	-	-	-	-	-
Mortgages	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-
Short-term investments	-	1.4	-	4,665.2	-	4,923.4
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-
Derivative financial instruments related to ABTNs	-	-	-	-	-	-
Demand deposits in the General Fund	-	2.6	-	177.2	-	-
	-	7,518.8	-	6,566.3	-	4,923.4
Other assets	-	11.6	-	4.1	-	3.9
	-	7,530.4	-	6,570.4	-	4,927.3
<b>Liabilities</b>						
Advances from the General Fund	-	-	-	-	-	2.1
Securities sold under repurchase agreements	-	-	-	-	-	-
Notes payable	-	4,920.6	-	4,115.7	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-
Loans payable	-	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-
Short selling of securities	-	49.7	-	1,194.6	-	-
Derivative financial instruments	-	37.0	-	93.6	-	207.6
Other liabilities	-	437.3	-	510.3	-	1.8
Non-controlling interests	-	-	-	-	-	-
	-	5,444.6	-	5,914.2	-	211.5
<b>Net holdings of funds</b>	-	2,085.8	-	696.2	-	4,715.8
<b>Consolidated income for years ended December 31</b>						
<b>Income</b>						
Investment income						
Real estate holdings	-	-	-	-	-	-
Equities and convertible securities	45.7	147.0	2.3	18.7	-	-
Bonds	-	-	-	-	-	-
Mortgages	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-
Short-term investments	-	0.3	3.0	24.0	33.1	118.1
Demand deposits in (advances from) the General Fund	-	(0.4)	-	1.0	-	(0.1)
	45.7	146.9	5.3	43.7	33.1	118.0
Other income	-	-	-	-	-	-
	45.7	146.9	5.3	43.7	33.1	118.0
Operating expenses	1.8	4.2	1.0	3.9	3.7	17.3
<b>Income before the following items</b>	44.2	142.7	4.3	39.8	29.4	100.7
Interest on loans and notes payable	33.1	118.1	4.5	37.2	-	-
Non-controlling interests	-	-	-	-	-	-
<b>Net investment income (loss)</b>	11.1	24.6	(0.2)	2.6	29.4	100.7
<b>Changes in consolidated net assets for years ended December 31</b>						
<b>Net investment results</b>						
Net investment income (loss)	11.1	24.6	(0.2)	2.6	29.4	100.7
Gains (losses) on sale of investments	(112.7)	(650.6)	(40.0)	(98.9)	(116.9)	309.3
Unrealized increase (decrease) in value of investments	-	-	-	-	-	-
and liabilities related to investments	177.8	888.0	83.3	191.2	(33.3)	0.1
Net investment results	76.2	272.0	43.1	124.9	(120.8)	410.1
Participation units issued (cancelled)	(2,150.8)	1,306.6	(699.5)	187.6	(4,565.6)	829.5
Net investment loss (net income) recovered from (allocated to) participation unit holders	(11.1)	(24.6)	0.2	(2.6)	(29.4)	(100.7)
<b>Increase (decrease) in consolidated net assets</b>	(2,085.8)	1,574.0	(856.2)	309.9	(4,715.8)	1,138.9
<b>Consolidated net assets, beginning of year</b>	2,085.8	511.8	656.2	340.3	4,715.8	3,576.9
<b>Consolidated net assets, end of year</b>	-	2,085.8	-	656.2	-	4,715.8
<b>Investments and liabilities at cost as at December 31</b>						
<b>Assets</b>						
Investments						
Real estate holdings	-	-	-	-	-	-
Equities and convertible securities	-	7,416.6	-	1,431.8	-	-
Bonds	-	-	-	-	-	-
Mortgages	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-
Short-term investments	-	-	-	4,697.3	-	4,682.4
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-
Demand deposits in the General Fund	-	2.6	-	177.2	-	-
	-	7,419.2	-	6,306.1	-	4,682.4
<b>Liabilities</b>						
Securities sold under repurchase agreements	-	-	-	-	-	-
Notes payable	-	4,680.4	-	4,036.0	-	-
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-
Loans payable	-	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-
Short selling of securities	-	47.3	-	1,016.9	-	-
Derivative financial instruments	-	0.1	-	7.4	-	-
Non-controlling interests	-	-	-	-	-	-

## SUPPLEMENTARY INFORMATION

## Summary financial statements for the specialized portfolios (cont.)

(in millions of dollars)

	U.S. EQUITY UNHEDGED (734) (Baudouin April 1, 2010)		COMMODITY FINANCIAL INSTRUMENTS (783) (Baudouin December 1, 2010)		INVESTMENTS AND INFRASTRUCTURES (791) (Baudouin July 1, 2010)	
	2010	2009	2010	2009	2010	2009
<b>Consolidated net assets as at December 31</b>						
<b>Assets</b>						
Investments at fair value	-	-	-	-	-	-
Real estate holdings	-	-	-	-	-	-
Equities and convertible securities	-	-	-	1,077.5	-	6,736.4
Bonds	-	-	-	-	-	943.3
Mortgages	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-
Short-term investments	-	4,115.7	-	-	-	2,882.0
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-
Derivative financial instruments related to ABTNs	-	-	-	-	-	-
Demand deposits in the General Fund	-	-	-	102.9	-	507.6
	-	4,115.7	-	1,180.4	-	11,069.3
Other assets	-	4.0	-	1,224.5	-	87.4
	-	4,119.7	-	2,404.9	-	11,156.7
<b>Liabilities</b>						
Advances from the General Fund	-	4.0	-	-	-	-
Securities sold under repurchase agreements	-	-	-	-	-	-
Notes payable	-	-	-	-	-	5,026.7
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-
Loans payable	-	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-
Short selling of securities	-	-	-	-	-	-
Derivative financial instruments	-	22.6	-	1,163.5	-	123.6
Other liabilities	-	-	-	4.2	-	85.5
Non-controlling interests	-	-	-	-	-	633.2
	-	26.6	-	1,167.7	-	5,969.0
	-	4,093.1	-	1,231.2	-	5,987.7
<b>Net holdings of funds</b>						
<b>Consolidated income for years ended December 31</b>						
<b>Income</b>						
Investment income	-	-	-	-	-	-
Real estate holdings	-	-	-	-	-	-
Equities and convertible securities	-	-	-	-	175.5	327.4
Bonds	-	-	-	-	17.5	59.1
Mortgages	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-
Short-term investments	4.4	37.2	-	1.5	50.5	116.4
Demand deposits in (advances from) the General Fund	-	(0.1)	0.1	(1.5)	0.6	(0.7)
	4.4	37.1	0.1	-	244.1	502.2
Other income	-	-	-	-	7.4	22.7
	4.4	37.1	0.1	-	251.5	524.9
Operating expenses	5.7	21.6	1.1	3.8	15.1	32.9
Income before the following items	(1.3)	15.5	(1.0)	(5.8)	236.4	492.0
Interest on loans and notes payable	-	-	-	-	45.5	129.6
Non-controlling interests	-	-	-	-	19.8	23.6
Net investment income (loss)	(1.3)	15.5	(1.0)	(5.8)	175.1	332.8
<b>Changes in consolidated net assets for years ended December 31</b>						
<b>Net investment results</b>						
Net investment income (loss)	(1.3)	15.5	(1.0)	(5.8)	175.1	332.8
Gains (losses) on sale of investments	148.1	366.6	68.3	685.9	(1,948.5)	38.8
Unrealized increase (decrease) in value of investments	(57.1)	22.9	(68.3)	(230.5)	2,381.1	954.7
and liabilities related to investments	89.7	405.0	(1.0)	89.6	607.7	1,325.8
Net investment results	(4,184.1)	1,832.9	(1,237.2)	(206.5)	(5,720.3)	21.4
Participation units issued (cancelled)	-	-	-	-	-	-
Net investment loss (net income) recovered from (allocated to) participation unit holders	1.3	(15.5)	1.0	5.8	(175.1)	(332.8)
Increase (decrease) in consolidated net assets	(4,093.1)	2,522.4	(1,237.2)	(111.1)	(5,287.7)	1,014.4
Consolidated net assets, beginning of year	4,093.1	1,870.7	1,237.2	1,348.3	5,287.7	4,273.3
Consolidated net assets, end of year	-	4,093.1	-	1,231.2	-	5,287.7
<b>Investments and liabilities at cost as at December 31</b>						
<b>Assets</b>						
Investments	-	-	-	-	-	-
Real estate holdings	-	-	-	-	-	-
Equities and convertible securities	-	-	-	730.8	-	9,118.8
Bonds	-	-	-	-	-	1,066.2
Mortgages	-	-	-	-	-	-
Mortgage securities	-	-	-	-	-	-
Short-term investments	-	4,036.0	-	-	-	3,294.5
Securities acquired under reverse repurchase agreements	-	-	-	-	-	-
Real estate held for resale	-	-	-	-	-	-
ABTNs	-	-	-	-	-	-
Demand deposits in the General Fund	-	-	-	102.9	-	507.6
	-	4,036.0	-	833.7	-	13,987.1
<b>Liabilities</b>						
Securities sold under repurchase agreements	-	-	-	-	-	-
Notes payable	-	-	-	-	-	5,290.3
Temporary funding attributable to foreign currency fluctuations	-	-	-	-	-	-
Loans payable	-	-	-	-	-	-
Mortgage loans payable	-	-	-	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-	-	-	-
Participating debenture	-	-	-	-	-	-
Short selling of securities	-	-	-	-	-	-
Derivative financial instruments	-	-	-	885.1	-	9.1
Non-controlling interests	-	-	-	-	-	1,017.8

**FINANCIAL CERTIFICATE OF THE  
PRESIDENT AND CHIEF EXECUTIVE OFFICER  
AND ACTING CHIEF FINANCIAL OFFICER**

I, Michael Sabia, President and Chief Executive Officer and Acting Chief Financial Officer of the Caisse de dépôt et placement du Québec, certify that:

1. **Review:** I have reviewed the Combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report (hereafter referred to as the "Annual Filings") of the Caisse de dépôt et placement du Québec (the "Caisse") for the year ended December 31, 2010.
2. **No false or misleading information:** To the best of my knowledge, having exercised reasonable diligence, the Annual Filings do not contain any untrue statement of a material fact or omit to state any material fact that is required to be stated or necessary to make a statement that is not misleading in light of the circumstances in which it was made, with respect to the period covered by the Annual Filings.
3. **Fair presentation:** To the best of my knowledge, having exercised reasonable diligence, the Combined financial statements and the other financial information included in the Annual Filings present fairly, in all material respects, the financial position of the Caisse as at the closing dates of the periods presented in the Annual Filings, as well as the results of its operations for those years.
4. **Responsibility:** I am responsible for the establishment and maintenance of disclosure controls and procedures (DC&P) and internal control over financial reporting (ICFR) for the Caisse, in accordance with the responsibilities entrusted to me under section 5.12 of the Caisse Act.
5. **Design:** Subject to the limitations, if any, described in paragraphs 5.2 and 5.3, as at fiscal year-end, I have:
  - a) Designed, or caused to be designed under my supervision, DC&P to provide reasonable assurance that:
    - i) Material information relating to the Caisse is made known to me by others, particularly during the period in which the Annual Filings are prepared.
    - ii) Information required to be disclosed by the Caisse in its Annual Filings filed or submitted by it under the legislation is recorded, processed, summarized and reported within the time periods prescribed by the legislation.
  - b) Designed, or caused to be designed under my supervision, ICFR to provide reasonable assurance that financial information is reliable and that the Combined financial statements have been prepared, with a view to publication of financial information, in accordance with generally accepted accounting principles in Canada.
- 5.1. **Control framework:** The control framework that I have used to design the ICFR is that proposed by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").
- 5.2. **ICFR material weakness relating to design:** Not applicable.
- 5.3. **Limitation of scope of design:** Not applicable.
6. **Evaluation:** I have:
  - a) Evaluated or caused to be evaluated under my supervision, the effectiveness of the DC&P of the Caisse at fiscal year-end and disclosed in its Annual Report my conclusions about the effectiveness of this evaluation.
  - b) Evaluated or caused to be evaluated under my supervision, the effectiveness of the ICFR of the Caisse at fiscal year-end and disclosed in its Annual Report the following information:
    - i) My conclusions about the effectiveness of the ICFR at the fiscal year-end based on that evaluation.
    - ii) Description of any material weakness relating to current operation at fiscal year-end: Not applicable.
7. **Reporting changes in ICFR:** The Caisse disclosed in its Annual Report any change in ICFR that occurred during the accounting period beginning on January 1, 2010 and ending on December 31, 2010 that has had, or is likely to have, a material impact on ICFR.
8. **Reporting to Auditors and the Board of Directors or Audit Committee:** I have disclosed, based on our most recent valuation of ICFR, to the auditors and the Board of Directors of the Caisse or its Audit Committee any fraud that involves management or other employees who have a significant role in the ICFR.

President and Chief Executive Officer  
and Acting Chief Financial Officer



**MICHAEL SABIA**

April 1, 2011

## **CONCLUSIONS ABOUT THE DESIGN AND EFFECTIVENESS OF INTERNAL CONTROL OVER FINANCIAL REPORTING**

In 2010, the Disclosure Committee oversaw efforts to update existing documents and evaluate the design and effectiveness of internal control over financial reporting. The evaluation of internal control over the Caisse's main financial processes aims at ensuring that the Caisse meets its quality objectives related to financial reporting, in all material respects.

The framework of the Committee of Sponsoring Organizations of the Treadway Commission (COSO) usually adopted by North American corporations was used to evaluate the design and effectiveness of internal control over financial reporting. This undertaking enabled the Disclosure Committee to conclude that the design of control over financial reporting is adequate and effective to provide reasonable assurance with respect to the reliability of the financial information presented in the Annual Filings, as defined in the Caisse's Financial Certification Policy, and that the Caisse's Combined financial statements are prepared in accordance with Canadian generally accepted accounting principles.

## **CONCLUSIONS ABOUT THE DESIGN AND EFFECTIVENESS OF DISCLOSURE CONTROLS AND PROCEDURES**

Under the Caisse's Financial Certification Policy, the design and effectiveness of disclosure controls and procedures pertaining to Annual Filings, i.e. the Combined financial statements, the schedules of returns, the press release announcing the annual results and the Annual Report, must be evaluated.

As with the evaluation of internal control over financial reporting, the Disclosure Committee oversaw efforts to update existing documents and evaluate the design and effectiveness of disclosure controls and procedures.

As at December 31, 2010, based on the evaluation, disclosure controls and procedures are adequate and effective, and provide reasonable assurance that all relevant information is gathered and submitted in a timely fashion to senior management, in particular to the President and Chief Executive Officer and the Acting Chief Financial Officer, to ensure that appropriate decisions concerning disclosure can be made.

The Board of Directors also approved the 2010 Annual Filings before their public disclosure.

# General Notes

1. The Caisse's activities comply with the requirements of the Act respecting the Caisse de dépôt et placement du Québec<sup>1</sup> and investment industry practices. Its financial statements are prepared in accordance with generally accepted accounting principles in Canada. Each year, the Caisse's co-auditors, the Auditor General and Ernst & Young (effective in 2010), audit the financial statements, the compliance of operations with the law, regulations, policies and guidelines to the extent they believe is required.
2. The 2010 Annual Report Additional Information is an integral part of the 2010 Annual Report and presents, in the first section, the "Tables of Returns" as at December 31, 2010, relating to the composites of the Caisse's depositors' accounts. The tables and calculations have been audited as at December 31, 2010, by the firm Samson Bélair/Deloitte & Touche s.e.n.c.r.l. for compliance with Global Investment Performance Standards (GIPS®).
3. The specialized portfolios' returns represent the time-weighted rate of return.
4. The benchmark indexes for the asset classes and overall portfolio are based on the weighted average of the benchmark indexes for the specialized portfolios.
5. Unless otherwise stated, returns are presented before operating expenses and other fees, but net of transaction fees. They include the return on cash and cash equivalents, and take into account, depending on the case, a hedge against currency fluctuation risk. The return variances related to the operating expenses of each specialized portfolio are presented in the Tables of returns of the 2010 Annual Report Additional Information.
6. Certain returns are expressed in basis points (b.p.). Therefore, 100 basis points equal 1.0% and one basis point equals 0.01%.
7. Unless otherwise stated, all figures are in Canadian dollars. The letters "M" and "B" used with dollar amounts designate, respectively, "millions" and "billions."
8. Totals (figures or percentages) may vary due to the rounding of figures.
9. Unless otherwise stated, all data in tables and figures are from studies conducted by the Caisse.
10. The tables listing the top 10 investments present, in alphabetical order, the main cash positions based on information shown in Tables 8, 9, 10 and 11 of the 2010 Annual Report Additional Information.
11. For many years, the Caisse has looked at the location of the company's or security issuer's headquarters in order to decide if it is Québec-based. For real estate, it refers to the location of the asset.

This classification system, which is generally used by the fund management industry, is not perfect. Some companies are considered as Québec-based, even if their core business is outside Québec, while other companies operating extensively in Québec are not taken into account if their headquarters is located outside the province.

1. The Act respecting the Caisse de dépôt et placement du Québec is available on our website.

- The 2010 Annual Report and the 2010 Annual Report Additional Information are available on our website: [www.lacaisse.com](http://www.lacaisse.com).
- Information: 514-842-3261, [info@lacaisse.com](mailto:info@lacaisse.com)
- *Le Rapport annuel 2010 et le document Renseignements additionnels au rapport annuel 2010 sont disponibles en français sur notre site : [www.lacaisse.com](http://www.lacaisse.com).*
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